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Competitive Marketing Strategy

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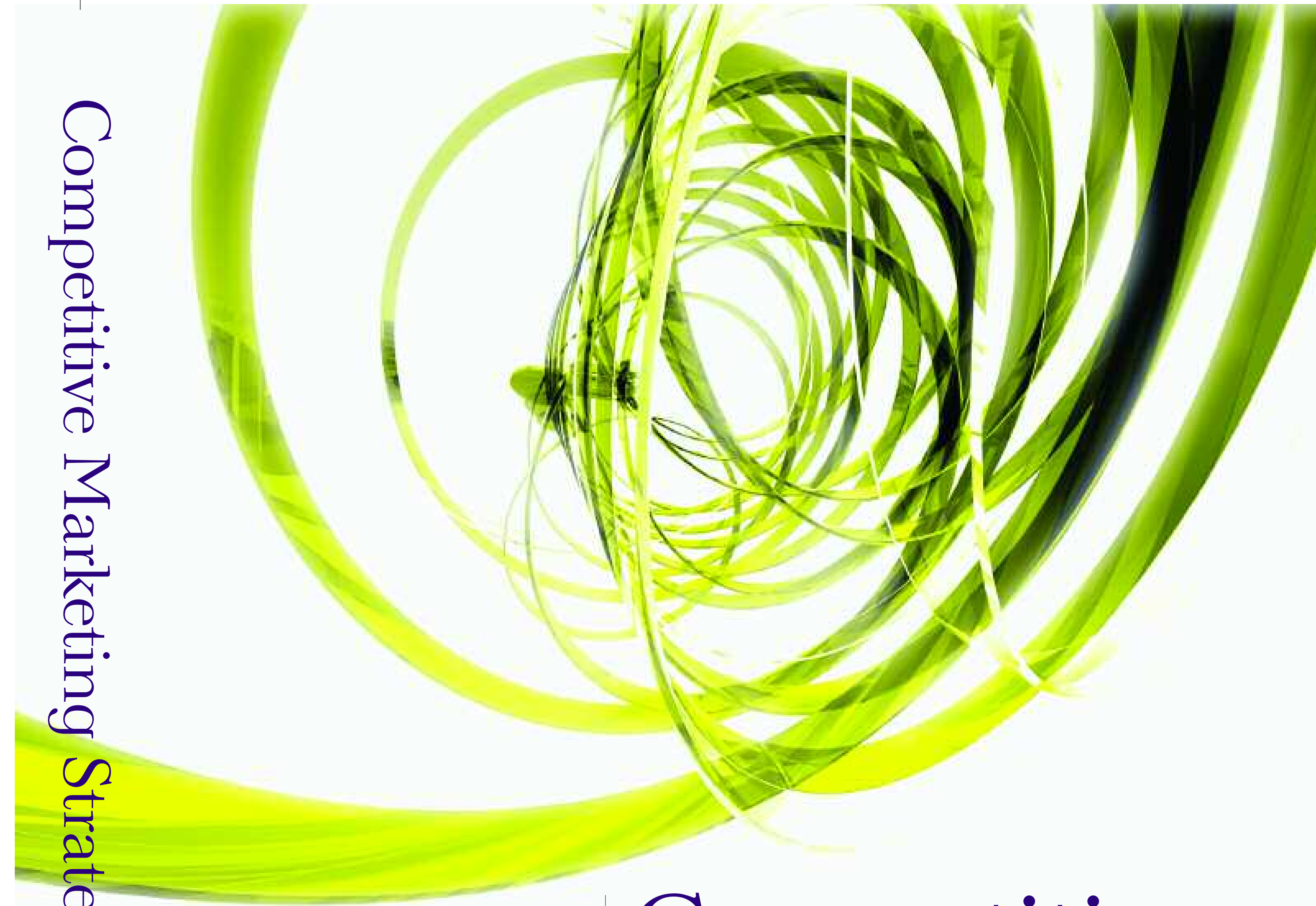

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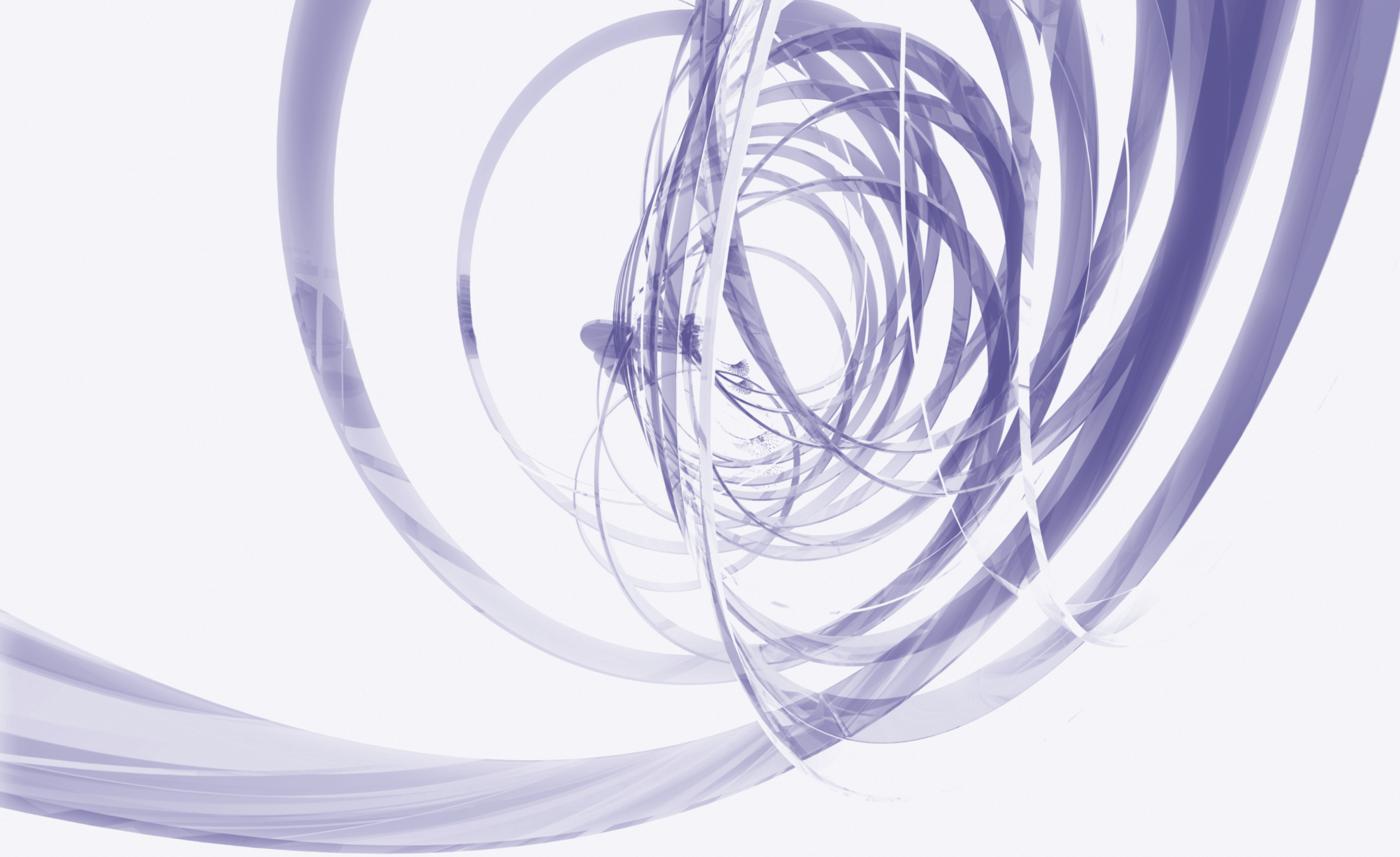

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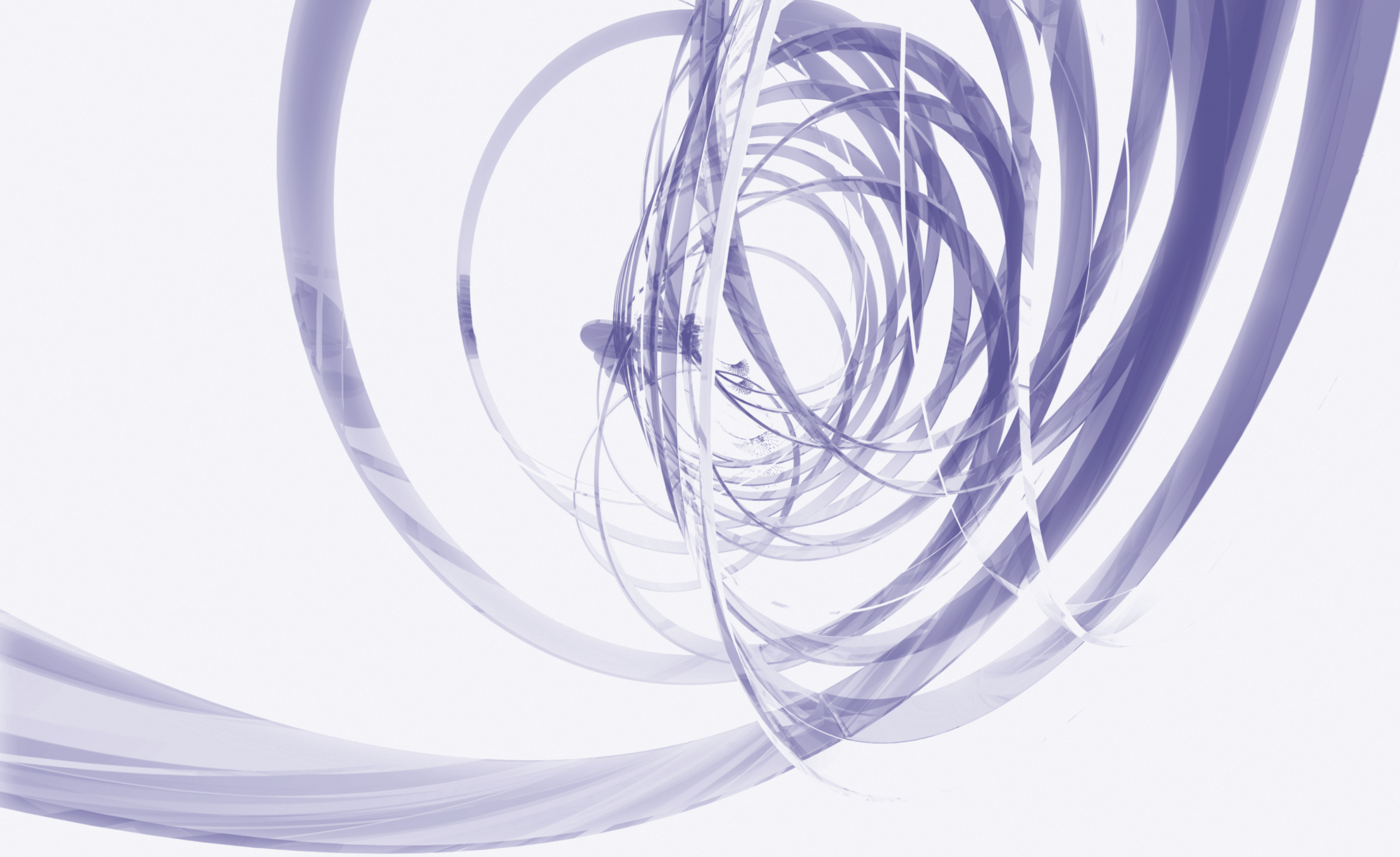

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This book is dedicated to everyone who will ever have to sit down and plan a strategy for an organisation. You'll need the dedication.

Contents

Part 3—Analysis into strategy

Part 4—Marketing implications

Preface

On strategy

Thus the highest form of generalship is to balk the enemy's plans; the next best is to prevent the junction of the enemy's forces; the next in order is to attack the enemy's army in the field; and the worst policy of all is to besiege walled cities.

SunTzu, *The Art of War*, www.chinapage.com/sunzi-e.html

The purpose of this book is to focus on the elements of marketing strategy that can be best communicated to the reader. Strategy is by no means entirely based on checklists, diagrams and words in a textbook. Whilst the book can show models, flowcharts and instructional ideas, strategy is about the application of these concepts in the dynamic environment of business. All the training in the world is no substitute for awareness of the market, and the willingness to see strategies implemented through tactics that deliver sales, revenue, market share gains or other objectives.

Consequently, there are few hard and fast rules of 'right' and 'wrong'. There are examples, there are recommendations of mental processes to follow, and there are codes of strategic conduct for a given situation, although these codes are more what you would call 'guidelines'. In the end, the best strategy is the strategy that suits the conditions of the market, the strength of the organisation and the ability of the company to deliver the strategic direction in concrete tactical actions.

Design decisions

Marketing strategy is an imprecise science at the best of times. This text is based on the assumption that each market, each value offering and each organisation is operating in a complex and varied market place. Consequently, there are no universal solutions, one-click applications or guaranteed outcomes. Instead, the book presents a series of conceptual frameworks, marketing strategies and market theories that the reader can use as the basis for examining, analysing and addressing their own unique strategic position. Even though every market is different, there are levels of commonality that can be used as a starting point for decision making.

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Thank you to the people who buy this book. It means a lot to us that you're going to be reading the end result of many hours at the keyboard, and many more hours of research, reading, learning and lost chances to be lying on the couch watching TV.

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About the book

The following section outlines the book and its individual chapters. Many of the concepts in the text are interconnected, and materials raised in one chapter may be repeated again later in the text. In educational terms this is a feature of the text rather than a flaw. In strategy, a recurring concept indicates the importance of the concept, so that the more often the idea appears, the greater the chance of it being crtical in business practice.

Part 1—Review of key concepts

The first part of the book covers areas that are assumed to be prior knowledge on the part of the reader. This initial section gives the reader a chance to briefly review (rather than learn) the key models, concepts and principles that underpin effective marketing strategy. The purpose of the section is to ensure that there is a common knowledge base and understanding of these concepts and models amongst the group prior to discussing specific strategic options. It is a useful starting point for any reader to pick up on any key knowledge that is missing or has been misinterpreted from earlier exposure. Those who are uncertain about any of the concepts covered in these first two chapters should consult a comprehensive introductory marketing or strategy text.

Chapter 1: A refresher in marketing

This chapter covers the basic concepts and definitions of marketing, the three levels of marketing and related areas such as consumer behaviour. This chapter sets out definitions and core concepts for revision with the assumption that readers have previously encountered this material.

Chapter 2: Review of key strategic models

Chapter 2 provides a selection of common strategic models and decision-making tools that students should have encountered at earlier stages of their degree program. The chapter includes an overview of:

- Ansoff's Growth Matrix
- the GE/McKinsey Matrix
- Porter's Five Forces
- Porter's Generic Competitive Strategies
- product life cycle.

Part 2—Doing the groundwork

The outcome of this section is that the reader should be able to carry out the processes needed to determine where the organisation currently sits, what its strengths and weaknesses are and what it is trying to achieve.

Chapter 3: Marketing and stakeholder selection

Chapter 3 is an overview of the issues surrounding the identification and selection of stakeholders. The concept that marketing strategies should be developed and implemented as a means of providing benefit for stakeholder value is an underlying principle and is embedded in later chapters. This chapter also includes an examination of the concept of shareholder value, an overview of value drivers and shareholder value analysis.

Chapter 4: Analysis 1—Internal analysis

This chapter provides a framework for internal analysis of the company using the balanced scorecard approach. The chapter will focus on the internal manifestations of the four elements of the balanced scorecard—financial, internal business issues, customer relationships and innovation—and outline how to assess each of these to give a full picture of the internal state of the company.

Chapter 5: Analysis 2—External analysis

Chapter 5 focuses on conducting an external analysis of the organisation with a specific focus on how the firm is positioned relative to the competition and the type of competitive environment the firm is operating in. Techniques for evaluating market attractiveness are also discussed.

Part 3—Analysis into strategy

This section examines the setting of objectives and discusses the implications of any specific choice for various marketing activities. Rather than take the traditional approach of discussing product strategy options, pricing strategy options and so on, this text takes a strategic marketing objective such as increasing sales in an existing market and then discusses what marketing strategies and marketing mix tactics would typically assist in achieving this objective.

Chapter 6: Strategic objectives

Chapter 6 gives a broad overview of different strategic options and the conditions under which these would be considered. Based on the broad strategic option chosen, for example, a growth strategy, it outlines the types of specific strategic objectives that fall within the category. This chapter also includes a discussion of the impact of segmentation strategies on the choice of strategic objectives.

Chapter 7: Growth strategy 1—Market penetration

Market penetration refers to the strategy of growth through either getting more customers from the same target market or getting existing customers to patronise the company more often. This chapter has a heavy focus on customer retention, loyalty programs and

relationship marketing strategies as a means of achieving market penetration. In addition, typical changes to marketing mix tactics, such as sales promotion and price discounting, are discussed.

Chapter 8: Growth strategy 2—Market development

Growth through market development involves the creation of a new market segment for the firm's product. Two options are discussed in detail in this chapter—repositioning strategies for existing products to appeal to new market segments and the development of international markets.

Chapter 9: Growth strategy 3—Product development

Product development involves creating new products to meet the needs of existing markets as the focus of marketing strategy. This chapter will include discussion of the new product development process and the impact of new technology and e-commerce in developing and redefining products. Also included in this chapter is a discussion of how different innovation adoption models explain consumer behaviour with respect to the marketing of new products.

Chapter 10: Value addition and strategic competitive advantage 1—Cost leader

Based on Porter's generic competitive strategies, this chapter focuses on cost leadership. Methods of obtaining cost leadership in different industries are discussed, along with the impact of cost leadership on pricing strategies. A focus of the chapter will be on the need to balance cost and value from the organisation's perspective with price and value from a consumer behaviour perspective.

Chapter 11: Value addition and strategic competitive advantage 2—Product differentiation

This chapter focuses on the critical importance of effective brand management in developing and sustaining competitive advantage. It discusses key issues in branding including the concept of brand as an asset, measuring brand value, managing a brand portfolio and re-branding or brand modification strategies.

Chapter 12: Value addition and strategic competitive advantage 3—Niche strategy

Chapter 12 discusses when, how and why niche strategies are used in preference to broader approaches to the market. Included in this chapter is a discussion of the different syles of niche segmentation, including mass customisation for 'segments for one'.

Chapter 13: Defensive marketing—Maintaining the position

Defensive marketing strategies are used to maintain current market position in situations when management have decided to avoid the temptation of growth or have determined that a strategic withdrawal from specific markets is in the longer-term interests of profitability. This chapter explores the importance of regularly reviewing the customer base and 'sacking' unprofitable clients to maximise returns to the firm. It also discusses the difficult issue of removing product or brands from the market without compromising the company and its reputation.

Part 4—Marketing implications

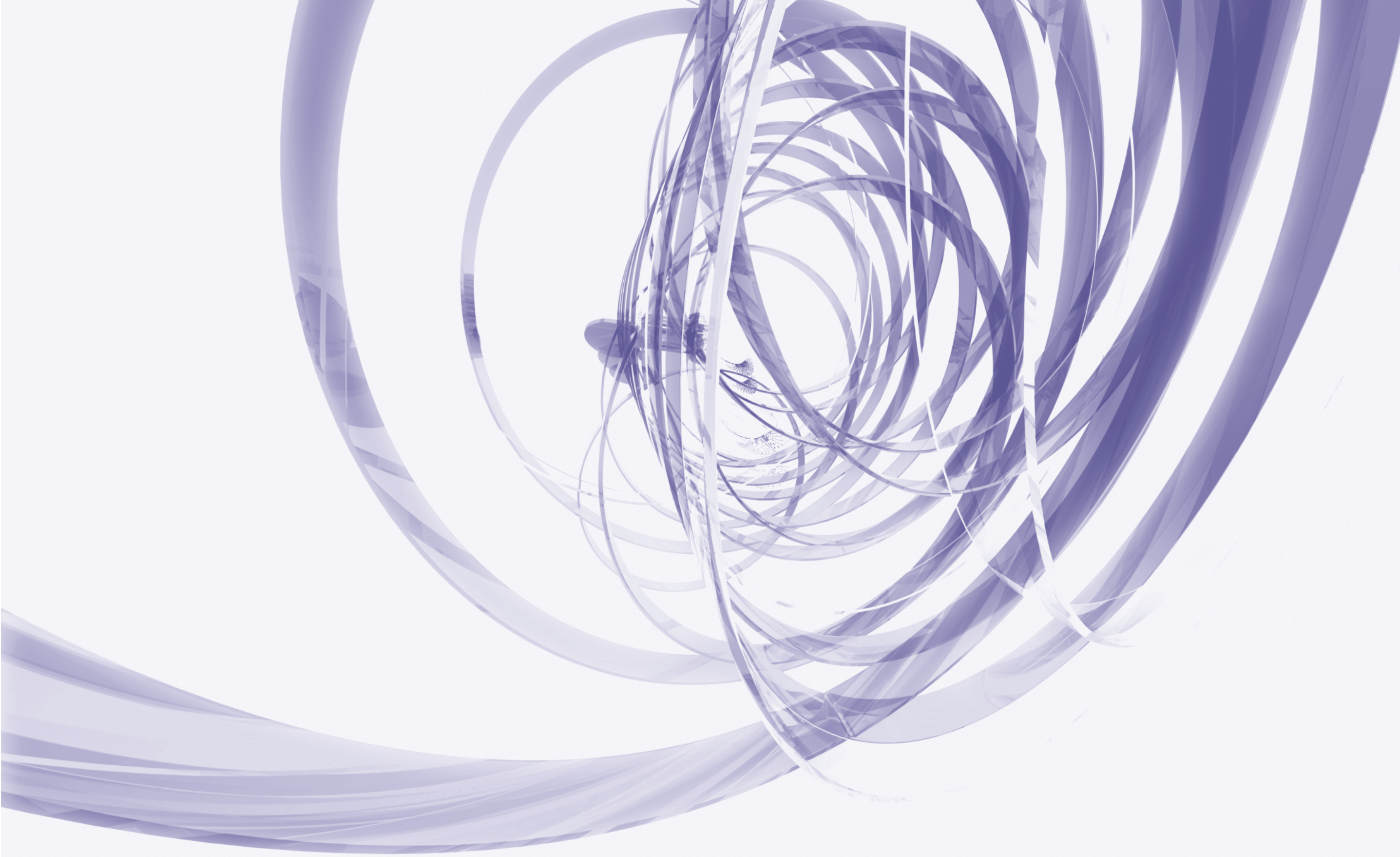
The final section of the book brings together the issues raised in the preceding chapters from a practical and managerial perspective. The focus of this section is to take the concepts and strategies from Parts 1 to 3 and bring them together into a strategic marketing plan.

Chapter 14: From analysis to action—The marketing plan

This chapter overviews the role and content of a strategic marketing plan and where it fits within the overall strategy of the company. It shows how to make sense of the analyses undertaken in the format of the marketing plan.

Chapter 15: Implementing the marketing plan

The final chapter gives guidance on the practicalities of implementing a strategic marketing plan. It includes a discussion on resource acquisition and allocation so that the plan can be implemented within the confines of the firm's capabilities. It also gives an overview of marketing metrics and how to report on, and demonstrate, the value of marketing within the organisation.

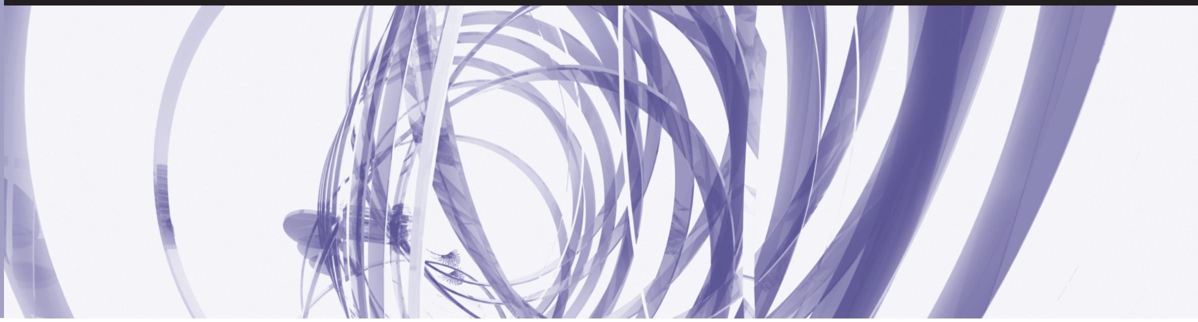


PART 1

Review of key concepts

A refresher in marketing

CHAPTER 1



Introduction

Competitive marketing strategy is a paradoxical aspect of modern business. At times, it relies on the instincts, skills and artistry of the marketer, yet at the same time, there is an expectation that the scientific rigour of market research, business statistics and economic measurement be applied in equal measure. As such, strategy is a technique that is an art form that is learnt best by doing, and a science that is learnt through models, theories and the analysis of existing knowledge. Although each business faces a different combination of circumstances in determining its strategic position, there are broad categories of existing knowledge and experience that can be used to assist the planning and implementation of strategy. As a consequence, competitive marketing strategy can be taught through the combination of the theoretical, practical and conceptual frameworks derived from the experience of other organisations in similar market conditions.

Guiding principles

The purpose of studying competitive marketing strategy is to learn to replicate the techniques that lead to success by studying the mistakes and successes of others. In general, marketing strategy has three core aspects:

- *Marketing is a cyclical process*, that is, aspects that were covered previously in the marketing process will often arise again in a slightly different context. Whilst this may initially appear annoying, in the sense that 'we've covered that', it is one of its strengths—knowledge gained in one part of the cycle can be used in the next part of the process.
- *Marketing is an ongoing process*. Marketing is often mistakenly regarded as something that is 'done', rather than something that should be an ongoing recurring part of the business cycle.
- *Marketing strategy is a fallible approach which relies on calculated risks*. Marketing can neither predict the market perfectly, nor have a total insight into the mind of the consumer. What it can do is quantify the processes, steps and decision-making procedures that lead to offering products to the market, so that later successes and failures can be analysed for patterns that can be repeated or avoided.

Marketing bootcamp

A textbook on strategic marketing faces strategic choices of its own: whether or not to assume a background knowledge of marketing. The difference in these two choices is dramatic, and underpins the design of the book and the selection of content. Where a text elects to assume no knowledge, it then undertakes to provide a wider range of information and resources per chapter, and per marketing concept. Each concept must first be explained, demonstrated in basic terms, and then applied to a strategic situation ('What it is, what it does, why you use it, and where it fits'). In contrast, the assumption of prior knowledge means that the focus is directed to the strategic applications of the concept. In this book, the reader is assumed to have prior working knowledge of marketing. Consequently, the book will provide the conceptual strategic framework, and emphasise the 'how and where' aspects of using marketing in strategy.

To assist the process, the first chapter of the book has been set aside as a revision of the core marketing concepts that will be used in the main body of the text. The chapter also briefly reviews the divide between the emphasis on relationship marketing and transactional marketing, and the value of the marketing mix in business and strategy.

Four basic conceptual areas of marketing will be overviewed, both as a refresher for the book, and to establish a common language. The four areas are:

- the definition of marketing
- relationship marketing and the marketing mix
- the philosophy, strategy and tactical levels of marketing
- the ethics of marketing.

Definitions of marketing

One of the problems facing marketing as a discipline is the multiple meanings assigned to various marketing terms, in both business and non-business language. The problem extends to the absolute basics of what constitutes 'marketing' as it is understood by practitioners, marketing writers and the general public.

The 2004 definition of marketing

The progression of the definition of marketing resembles that of an atomic half-life—the first definition stood for 50 years, the second was revised within 19 years, and the American Marketing Association (AMA) leadership has speculated that the current definition will be revised again within five years (AMA 2004). The most recent formal definition of marketing, as unveiled by the AMA (and endorsed by the global marketing community) defines marketing as:

> an organizational function and a set of processes for creating, communicating and delivering value to customers and for managing customer relationships in ways that benefit the organization and its stakeholders. (AMA 2004)

Previously, the definition of marketing was:

> the process of planning and executing the conception, pricing, promotion, and distribution of ideas, goods, and services to create exchanges that satisfy individual and organizational objectives. (AMA 1985, p. 2)

The changes between the two definitions are significant, and represent a major change in the role of marketing. Marketing is now an organisational function and process, whereas it was previously perceived predominantly as a process. This reflects the growth of dedicated marketing functions within organisations, and also demonstrates the broader acceptance of marketing as an equal to accounting or research and development. Second, the new definition no longer explicitly recognises the marketing mix, and instead focuses on the concept of 'value creation' for the firm and for the customer. Gone is the explicit focus on creating exchange as the core of the marketing definition—value is now the core of marketing. In addition, the notion of satisfying individual and organisational objectives has been traded for managing customer relationships in ways that benefit the organisation and its stakeholders.

Broadly speaking, the revision of the definition moves marketing away from the shorter term transactional-exchange orientation and into an area which has a greater emphasis on the longer-term relationship, value and stakeholder benefit. This represents a shift in the methods of marketing thought and strategy—marketing is now a relationship, based on the creation of value for customers and benefits for the organisation and stakeholder where it had previously been an exchange between two or more parties.

There are three core components of the marketing definition:

- organisational function
- a set of processes for creating, communicating and delivering value to customers
- a set of processes for managing customer relationships in ways that benefit the organisation and its stakeholders. (AMA 2004)

Organisational function

Marketing as formally defined by the AMA (2004) requires a specific function and role within the organisation. Loosely translated, this can range from having a fully-fledged marketing department, through to having an individual staff member responsible for the organisation's marketing activity. The explicit recognition of a marketing organisational function assists marketing in defining and defending its territory against other disciplinary areas such as communications or journalism. It also represents a significant shift from the 'marketing is everything, everything is marketing' mindset of the 1990s, where the organisational marketing orientation required the whole of the organisation and just about every staff member to consider themselves part of the marketing process.

A set of processes for creating, communicating and delivering value to customers

The second component of the marketing definition is to formally recognise the composition of marketing as a series of procedures, rather than just a departmental function. This consists of:

- creating value, which is the process of translating the knowledge of the needs and wants of a market into specific product offerings
- communicating value, which is the process of using the marketing promotional mix to talk to the target market to explain the match between the value offering and the needs of the market
- delivering value to the customer, which involves using distribution channels to physically relocate the value offering from the point of production to the customer.

Value

Value is a complex aspect of the marketing definition, with multiple definitions of the term being used throughout the marketing process. As a consequence of this variation, during the course of this book the term is used in multiple ways depending on its context. At the most common level, value is defined in financial terms, either as the return on investment over time (lifetime value) or the cash price for a product (value offering to the customer), from the point of view of the organisation (e.g. lifetime value of the customer), the customer (e.g. value offering) and the stakeholders (e.g. shareholder value). From the point of view of the marketing definition, value is defined as the benefits received by the consumer from the product offering, in return for either non-financial (time, effort) or financial (cash) investment. Customer value is a subjective factor which has to be based on the customer's needs and wants, rather than imposed by the organisation. Although the language of

'creation, communication and delivery' may imply some form of top-down approach to value creation, ultimately value is derived from understanding the needs of the customer and developing an offer in response to those needs.

Processes for managing customer relationships in ways that benefit the organisation and its stakeholders

Organisation and stakeholder benefit

The third aspect of the marketing definition broadens the role of the marketing orientation beyond the dynamic between client/customer and the organisation. The expansion of the concept to include stakeholder benefit as an explicit role of marketing impacts on the type and nature of the strategies that can be defined as marketing strategy.

Core marketing strategy decisions: defining the stakeholders

A core strategic imperative to arise from the marketing definition is the need to define the organisation's stakeholders. Freeman (1984) defines stakeholders as 'any group or individual who can affect or is affected by the achievement of the firm's objectives'. This is a considerable difference to the more narrow view of stakeholders as shareholders, stockholders or owners of the organisation (Clement 2005). From the point of view of Waddock, Bodwell and Graves (2002) stakeholders are split into two categories:

- *primary stakeholders*: those who are needed for the ongoing survival of the organisation, including shareholders, employees, customers and suppliers
- *secondary stakeholders*: those not involved in transactions with the organisation and who are not essential for the survival of the organisation. These include non-governmental organisations (NGOs), activists, communities and governments.

As a result of the 2004 marketing definition, contemporary marketing strategy has to be developed in light of managing the customer relationship for the benefit of the organisation and the organisation's stakeholders. The definition of 'stakeholders' is now a critical element in determining what marketing can do to create benefit for the organisation and the stakeholders. Mitchell, Agle and Wood (1997) propose a three-part model to determine the relative importance of stakeholders. In their model, each stakeholder is assessed according to the following criteria:

- *power*: the extent to which the stakeholder can assert their will over the organisation. For example, government stakeholders will be more frequently addressed ahead of other groups, since the government can enforce its will through law.
- *legitimacy*: the appropriateness of the stakeholder's actions towards the firm, whether they are desirable, within socially accepted norms, or consistent with wider society expectations. Lobby groups and pressure groups range in legitimacy. For example, a lobby group pressuring a car manufacturer to reduce the exhaust emissions created by new cars will be seen to have greater legitimacy than if the same lobby group called for the cessation of car manufacturing.

- *urgency:* the degree to which the actions of the stakeholders require an immediate response, or the degree to which the response is time sensitive in nature. For example, protestors and television cameras in the reception require more immediate action than a series of letters to the editor of a newspaper. Similarly, time-sensitive issues, such as addressing concerns regarding product safety or dealing with crisis management issues, create urgency.

Agle, Mitchell and Sonnenfeld (1999) further argue that the three elements should receive different weighting in terms of their relative impact. They suggest that power be given the highest weight, followed by urgency then legitimacy. For example, a large lobby group (power) with a current media campaign (urgency) will weigh in as an important stakeholder, even if the claims in their campaigns may be inaccurate (legitimacy). In the most extreme case, a product poisoning scare, such as that experienced in 2005 with Mars and Snickers bars shows the importance of power (poisoned products) and urgency (immediate need to act to recall and destroy product) even where the actions of the person were completely illegal (lack of legitimacy). Whilst the power model in this form is a defensive measure, it is also strategically limiting as it requires the company to view stakeholders as threats (power, urgency, legitimacy) rather than opportunities (legitimacy, urgency, power). Even when a stakeholder holds limited power and there is little urgency, there may be a legitimate cause that could be addressed to the benefit of both organisation and stakeholder. The issues of stakeholder identification and the strategic impact of stakeholder selection will be examined again in Chapters 3, 4 and 5.

Relationship marketing and the marketing mix

Even without the explicit recognition of the value of ongoing customer relationships within the marketing definition, relationship marketing has been a cornerstone of marketing theory for nearly two decades. This section provides a brief overview of the core concepts of relationship marketing and a discussion of the role of the marketing mix in the era of relationship marketing.

Relationship marketing

Relationship marketing rose to prominence in the 1990s, offering an alternative to the transaction/repeat transaction focus of the marketing mix. Grönroos (1990) defined relationship marketing thus:

> Marketing is to establish, maintain, and enhance relationships with customers and other partners, at a profit, so that the objectives of the parties involved are met. This is achieved by a mutual exchange and fulfilment of promises. (p. 138)

Grönroos (1994) saw the marketing mix as limiting marketing creativity and decision making to a narrow parameter of simply adjusting elements of the mix. As a contrast to this approach, he offered the alternative idea that relationship building and management could

replace the emphasis on transaction-based marketing. Since the seminal work of Grönroos (1990, 1994), the once-coherent concept of relationship marketing has fractured, with numerous authors putting forward 'definitive' definitions of relationship marketing. For the purpose of this book, the following areas of relationship marketing will be examined:

- the lifetime value of the customer, which is the reason to engage in an ongoing relationship
- the assumption that customer loyalty does exist, and that it can be reinforced or influenced by relationship marketing
- the principles of trust, reciprocity and commitment, which form the basis for a commitment to a longer-term relationship
- the idea that relationship marketing may not be universally applicable in business (a concept which needs further consideration due to the inclusion of relationship management as a core of the definition of marketing).

Lifetime value of the customer

Customer lifetime value is the difference between the costs of attracting, keeping and servicing the customer against the revenue generated by those activities. Berger and Nasr (1998) provide a comprehensive overview of a set of generic models for calculating customer lifetime value, including a range of complex formulae designed to offer objective methods of assessing lifetime value. In this model, they describe customer lifetime value as the net contribution margin achieved per customer, once the customer has been acquired. Berger and Nasr acknowledge that their model does not include the cost of acquisition of the customer. Instead, they compute the value based on the difference between the revenues and the cost of sales and promotion expenses. Cost of sales includes logistics, distribution, cost of manufacturing and handling and shipping. Promotion costs are those costs associated with loyalty schemes, general promotional activity excluding promotions specifically designed to recruit new customers, and general image enhancement campaigns (e.g. sponsorships, PR, or other brand enhancement activities). In effect, the Berger and Nasr model assesses the customer lifetime value on the basis of all expenditure (excluding new acquisition costs) against the ongoing revenue from the existing customers (excluding revenue from new acquisitions until they become ongoing). As a result, their models can be used to assess the long-term viability of the customer relationship and the firm's sales strategy.

Principles of relationship marketing: trust, commitment and reciprocity

Relationship marketing depends on the principles of trust, commitment and reciprocity, which are defined as follows:

- *Trust* is the willingness to rely on a partner in an exchange, including the level of confidence in the other partner, belief in the trustworthiness and the reliance on the other partner to perform (Moorman, Deshpandé & Zaltman 1993, Grönroos 1994).

- *Commitment* is the perceived need to continue the relationship, either due to the inherent value of staying or the cost of departure (Geyskens et al. 1996)
- *Reciprocity* includes the notions of equality in the transaction, value-for-value exchange and the mutual obligation between partners in the relationship.

Issues associated with trust

Relationship marketing requires the creation of trust between the parties involved in the transaction. The use of trust as a construct to be built through deliberate and strategic activity can be perceived as an unethical element of marketing. However, in the context of business relationships, trust is defined as a calculated measure of the risk of engaging in the transaction, and is less dependent on the emotional elements connected to interpersonal trust. Consequently, trust can be calculated, assessed and deliberately modified by strategic decisions. Doney and Cannon (1997) outline five processes for trust formation, which are:

- *calculative processes* in which both parties assess the economic value of cheating or defrauding the relationship and where the cost of being caught is measured against the value of cheating. The value of cheating in turn is assessed against the value of non-cheating behaviour. Where the value of cheating exceeds the value of non-cheating, and/or is greater than the cost of being caught, cheating behaviour can be expected.
- *prediction of future behaviour based on past behaviour*, which assesses the risk of cheating behaviour against the previous behaviour of the relationship partner. A transaction partner with a history of cheating behaviour should be expected to continue that behaviour.
- *credibility*, or the level of trust generated by the apparent capacity and capabilities of the relationship partner to deliver on their promises. Trust is influenced by the level of risk apparent in choosing to rely on this business partner, and this is moderated by the extent to which the partner can obviously meet the obligations of the relationship.
- *motive assessment*, or the interpretation of the motives of the other partners in the relationship. This is a more subjective measure, and assumes relatively high levels of transparency which make it obvious when the other partner is acting against the best interests of the relationship.
- *transference*—a process which occurs where trust is developed by reputation from word of mouth, positive reviews, industry awards or external accreditation.

Trust in the commercial relationship has strategic implications beyond the development of marketing relationships. For example, a company with a propensity to engage in cheating behaviour in relationships will have to contend with the word of mouth/transference process in other areas of its marketing—such as promotion, public relations and corporate image. Similarly, if an organisation sets a strategic goal to be perceived as trustworthy by key stakeholders, the goals and activities of the organisation must be consistent

with what those key stakeholders regard as 'trustworthy'. For example, a clothing company may decide to raise the levels of trust with its customer base by only importing non-sweatshop labour clothing. However, that may not raise trust if the customers perceive the company to be exploiting workers in some other aspect of its business (e.g. pay disputes with shop staff).

Issues associated with commitment

Commitment is the goal of relationship marketing and one of the fundamental goals for marketing under the 2004 definition. Commitment is dependent on service/product quality and satisfaction, which relates to whether or not the organisation delivers the value they communicated to the customer. Satisfaction is also based on whether the needs of the consumer are being met (value being delivered). Morgan and Hunt (1994) split commitment into two facets—affective commitment and calculative commitment. Affective commitment refers to the emotional elements of the relationship, such as liking, sense of bonding, emotional attachments and subjective preferences for the relationship. Calculative commitment is the economics of commitment as an assessment of gains, losses, benefits and costs associated with a continuing or existing relationship.

Issues associated with reciprocity

Reciprocity is the mutual exchange and fulfilment of promise where the totality of the exchange balances out over the course of the relationship. Unlike transactional marketing, where the reciprocity of the exchange must occur immediately, relationship reciprocity can occur over the longer term. Relationship reciprocity involves the non-monetary aspects of the marketing relationship and includes:

- increased stability between relationship partners
- reduced risk in supplier selection; and
- increased efficiencies over the course of the relationship.

Reciprocity is the key element of the lifetime value of the customer—if reciprocity is not present, the relationship will either be dissolved by the customer, or need to be exited by the company if the customer relationship has ceased benefiting the organisation and its stakeholders.

Suitability of relationship marketing

Relationship marketing, like transactional marketing, is not a universal solution. Sometimes a customer will just want one product in a quick exchange, and will not be seeking an ongoing commitment to the organisation. Other times, whilst the customer may want the commitment, it may not be in the best interests, tactically or strategically, of the organisation to develop longer-term relationships. As the 2004 definition points out, marketing is about managing the relationship in ways that benefit the organisation and stakeholders. The termination of an unprofitable relationship is acceptable if it will bring benefit to the organisation. Gilbert, Powell-Perry and Widijoso (1999) created a six-point checklist to assess where relationship marketing is most suited. These six points are:

- *The customer has an ongoing or periodic desire for the product or service.* This is why providers of fast moving consumer goods (FMCG) tend to form relationships not with their end users, but with retailers. An individual may not need a chocolate bar every day, but the retailer is guaranteed to be selling someone a chocolate bar every day.
- *The service customer controls the selection of the service supplier, so that the relationship can be created.* Whilst the product user may want to be loyal and build a relationship with the supplier (e.g. continue using HP computers), their organisation may require the use of the lowest price tender, or other mandatory purchasing policies may prevent the development of ongoing relationships with the supplier organisation.
- *There are alternatives in the market.* Monopoly conditions do not require relationships, since the customer has no choice in the matter.
- *Brand switching is common, but can be prevented or minimised.* Relationship marketing becomes a strategic decision, where the emphasis is on holding existing customers in profitable relationships ahead of other strategies such as developing new markets.
- *Word of mouth and the transference process are important parts of the communication strategy in the market.* This creates an environment where relationship marketing is a communications function as well as a revenue source. Satisfying current recurring customers with relationship marketing will encourage positive word of mouth, and expand the potential customer base through referrals from existing customers.
- *There is an ability to cross-sell products once the relationship is established.* A large part of the lifetime value of a customer is the ability to expand the customer's involvement with the organisation from the original product (e.g. bank account) into ancillary related products (home loan, credit card). This has the dual effect of increasing switching costs and increasing the level of revenue received from the relationship. It also supports the market penetration strategy.

Strategic impact of relationship orientation

Relationship marketing requires the organisation to place a level of value on its customer and on the ongoing relationship with that customer. This approach will influence strategic decision making, and also be influenced by the strategy selection of the organisation. For example, relationship marketing is best suited to customer satisfaction, market penetration and product development strategies, all of which focus the activity of the firm on existing markets. The impact of relationship marketing on various types of strategies will be examined in Chapters 7–13.

The marketing mix

The marketing mix is, and should always be, considered a teaching tool used to demonstrate the core principles of marketing. Although there have been numerous criticisms of

the mix over time, it does remain a useful element of marketing. In quick summary, the core marketing mix is defined as:

- *price*: the cost to the consumer incurred by acquiring and using the product, including the financial costs of consumption as well as the non-financial social costs of time, effort, psyche, risk and social prestige
- *product*: the total package of benefits created by an organisation to offer to a target adopter
- *promotion*: the use of the audio and visual communication elements of marketing for the purpose of getting a message to the marketplace
- *place*: the distribution mechanism used for taking the product from the point of production to the consumer (and possibly the point of consumption).

Over time the mix has been further developed and extended to include such elements as:

- *people*: representing the role of the employee and the customer in the marketing exchange process
- *process*: the procedures, mechanisms and flow of activities by which services are consumed
- *physical evidence*: the environment in which the service is delivered, including tangible goods that help to communicate and perform the service.

The purpose of the 4Ps or 7Ps of marketing is to act as a mental checklist for the marketing strategist and practitioner so that the core elements of the offering to the market can be easily recognised by the consumer. Rather than being the sum total of marketing theory and practice, the marketing mix should be used to double-check that the key ingredients are covered—the question of what value proposition you are creating, communicating and delivering to the customer can be answered by checking the marketing mix. For example, determining the value proposition means asking what the product is (product), what it costs (price), where the consumer can purchase/use/experience it (place), and whether the consumer has been informed about the value offer (promotion).

The mix in the 2004 definition

Even though the 2004 definition of marketing removes the explicit statements of the marketing mix which were in the 1985 definition, the presence of the mix is still evident as the purpose of marketing is to create (product), communicate (promotion) and deliver (place) value to the consumer. Unfortunately, price is less explicitly present in the new definition, which merges the role of product and price in the concept of 'value'. This does not negate the need for marketing to examine the impact of price in marketing strategy. It does however place emphasis on merging the non-financial aspects of pricing, such as implied prestige, with the intangible elements of the augmented product, such as social status, to create a total 'value' for customers.

Three levels of marketing

Marketing exists as a business philosophy, a strategic framework for business decisions, and a series of tactical measures used at the implementation level. The philosophy of marketing can influence the selection of a strategy and the chosen strategy will impact on the tactical level use of marketing. Understandably, there are some areas of overlap and confusion between the three levels.

Philosophy

At the core of the philosophy of marketing are the two assumptions; the virtue of capitalism, and the primacy of individual choice. Marketing is deeply rooted in the philosophic structure of capitalism, and as such, is an aspect of capitalist society which may not be appropriate or applicable to non-capitalist social structures. In addition, the fundamental nature of marketing as a relationship between customer and organisation, and the notion of delivering value to the consumer, emphasises the individualistic nature of the consumer. Including recognition of the benefit to the stakeholders broadens the role of marketing benefits beyond the consumer–producer dyad. However, the emphasis is still on providing value for benefit between organisation and individual.

In terms of a business philosophy, marketing looks at putting the customer's needs at the centre of the business decision-making model, so that the organisation focuses on the creation, communication and delivery of value to that consumer, while still providing benefit to the organisation and stakeholders. Survival of the organisation is based around the assumptions that the relationship with the customer will be of benefit to the organisation, and that the communication, creation and delivery of value to the customer is achieved at an acceptable level of cost-recovery and/or profit.

The marketing philosophy impacts on the broader range of strategies that are available to the organisation to enable it to pursue a customer-centric goal. In many respects, marketing's customer-centric focus is in conflict with strategies designed to maximise shareholder value, operational excellence or innovation leadership. Sometimes, what the customer wants is contrary to the organisation's objectives. However, at the core of all business strategy is the notion of generating revenue, which relies on at least some form of satisfaction of customer needs. The question of how much influence those customer needs have over the overall strategic direction of the firm is answered by the extent to which the organisation adopts a marketing philosophy.

Marketing strategy

The marketing strategy orientation towards business again puts the needs of the customer at the centre of the decision-making process. It relies on:

- information gathering to understand the needs of the customer, which involves internal analysis for current customers (Chapter 4) and external analysis for potential customers (Chapter 5)

- monitoring of competitive environments to determine where the consumer could satisfy those needs (Chapter 5)
- decision making regarding what products to create, which markets to serve, how to best communicate the value offering, and the positioning of the firm in the market (Chapter 15)
- translating the philosophy into practical frameworks and strategic guidelines that can be used to develop the tactical-level implementation, including objective setting (Chapter 6), marketing plans (Chapter 14), and strategy setting (Chapters 7–13).

Tactics

Marketing tactics are the implementation of marketing strategies at the operational level of setting prices, delivering products and engaging in marketing communications. At the tactical level, marketing is concerned with market research, adjusting the marketing mix and building the practical relationship marketing elements. Included in this level are elements such as loyalty programs, the selection of distribution channels, the use of marketing communications and the promotional mix. Finally, the tactical level is where the sales are made, the revenue gathered and the product delivered to the consumer. Whilst this book does not address the tactical level directly, reference will be made to the types of tactics that may assist the implementation of the strategy.

Ethics of marketing

At the core of the 2004 marketing definition is the exploitation of the relationship between consumer and organisation for the benefit of the organisation and stakeholders. Although this is a harsh assessment of the definition, the reduction in emphasis on exchange between consumer and organisation does shift the power balance. Whilst the consumer is to receive 'value' as part of the process, the management of the relationship is based on benefit flowing to the organisation. Where the benefit does not exist, it would be expected that the relationship would be terminated, even if the customer is still gaining value. Unfortunately, however you view marketing, the fundamental nature of the process is that the organisation has to act in its own best interest, and is not expected to be a philanthropic entity.

That said, one of the common criticisms of marketing as an exploitative process does neglect to assess the nature of the consumer in the process. Although the purpose of the marketing relationship is to provide benefit to the organisation, it can only be marketing if the organisation is providing value to the consumer. Once the consumer makes a conscious decision to become part of the process by accepting the value offer, they are a player in the exchange process, and should be recognised as such (Carson, Gilmore & MacLaran 1998).

Generic criticisms of marketing

There are five generic criticisms of marketing that should be considered when setting strategy for the organisation. These criticisms are:

- Marketing is unfair. This is based on the unavoidable outcome of several strategies that involve calculated efforts to optimise a value offering to a market. Relationship marketing also encourages marketing to focus preferential treatment on some consumers at the expense of others.
- Marketing is manipulative. This criticism is both overstated in terms of just how effective marketing methods are in influencing consumers, and justifiable in that marketing is meant to have a manipulating effect. Relationship marketing was developed as a method to manipulate customer loyalty into ongoing revenue. Similarly, the communications methods of marketing are designed to either manipulate brand switching or brand loyalty desires. However, marketing is still an inexact science, and as such is not a perfect manipulative technique.
- Marketing is wasteful. This criticism is predominantly aimed at the tactical level of packaging and product development. However it is worth keeping in mind when examining strategy choices. Should your organisation focus on sustainable resource use and development when determining market development, growth or new product development strategies?
- Marketing plays favourites. Marketing, by the nature of using techniques such as market segmentation, will always play favourites. This is more a feature than a criticism, although with the broadening of the definition to include the wider stakeholder base, marketing will need to consider not just its 'favourites', but the wider stakeholder groups. This criticism will impact most heavily on niche marketing and brand leadership strategies, and will be addressed again in Chapters 11 and 12.
- Marketing is intrusive. This criticism is usually addressed at market research and direct marketing, but can also realistically be seen to apply to the ever-increasing presence of marketing and marketing tactics in the community.

Core concepts to refresh

One of the determinants of the success of a marketing strategy is recognising, and addressing, the influence of key marketing concepts on strategic outcomes. In other words, when designing a marketing strategy, there are several common elements of marketing that have a significant influence on the success or failure of any strategy. For the purpose of this book, the core concepts to be refreshed are:

- marketing orientation
- differentiating business to business and business to consumer
- the consumer decision process
- innovation and innovation adoption
- segmentation, positioning and branding.

The value of briefly revising these areas is twofold. First, it gives a common frame of reference between author and reader to establish that both parties are working from the

same sets of assumptions and concepts. Second, these concepts exert varying influences on the strategic marketing process. The decision to launch a new product into a new market should only be considered where the organisation has a grasp of the innovation adoption process of the consumer. Similarly, niche marketing strategies are heavily dependent on a concrete understanding of segmentation and positioning.

Marketing orientation

Kohli and Jaworski (1990) define the marketing orientation as the activities involved in the implementation of the marketing concept, where the marketing concept is the philosophy or way of thinking that guides the allocation of resources and the formulation of strategies for an organisation. For the purposes of this text, the marketing orientation is understood as the organisation's focus on matching the ideals and values of the marketing definition (creation of value for customers, benefits for organisation and stakeholders) through strategy and business practice. It relies on the balance between genuine value creation for the customer, and the need for the organisation to draw benefit from the relationship with the customer. At no point does a marketing orientation allow for either the marketer or the customer to dominate the relationship.

Marketing orientation is an important aspect in determining the overall strategic direction of the firm. Where the firm has a strategic focus on meeting the needs of the customer and the stakeholders it will select different goals and outcomes compared to an organisation focused on maximising shareholder returns, or one based on rapid market growth and expansion. Chapters 3 and 6 discuss the impact of objectives and strategic focus in greater detail.

Six-step model of marketing orientation

Carson, Gilmore and MacLaran (1998) propose a six-step model of the philosophy of the marketing orientation, based on the assumption that both consumer and organisation are active participants in the marketplace, and that both parties are acting to further their best interests. Their six-step model is as follows:

- Focus the marketing on honesty, frankness and openness in communications.
- Focus on marketing for profit.
- Build a marketing message that explicitly recognises that the company is trying to sell something to the customer, and that they aim to persuade the customer to buy from them.
- Treat the customer as a player in the game of exchange.
- Recognise that the customer has their own agenda and objectives.
- Explicitly recognise that the customers want the best for themselves, the organisation wants the best for itself, and both parties are trying to achieve the maximum gain for themselves.

The core of the six-step model is to act openly and respect the consumer, and to recognise that consumers are not hapless victims waiting to be exploited, but consenting participants in the marketplace. This notion of the consumer as participant also helps raise

the expectations of the marketplace, and increase the likelihood of the organisation acting ethically. Where the consumer is seen as somehow powerless, a victim, or just plain stupid, the organisation's contempt for its customer will inevitably influence its marketing and strategy. In contrast, respect for the customer is more likely to develop into an ongoing, exchange between the customer and the organisation. This idea of respect for the customer is partly captured in the new marketing definition's emphasis on 'managing customer relationships', given that core principles of relationship marketing require levels of respect, trust and reciprocity between customer and firm.

Differentiating business to business and business to consumer

At the very core of the strategic decisions will be the choice of targeting consumers or businesses as the primary customer base. Whilst some overlap exists between consumer and business to business (B2B) marketing, these areas are usually regarded as requiring distinct strategies. In particular, product purchasing in the business sector differs considerably from the consumer market. Business to business purchasing is a whole category of research in itself, and students planning a career in the field are advised to read more about relationship marketing and related fields.

The major differences between consumer purchasing and business purchasing that can impact on the selection of business strategies are that businesses often rely on stricter standards and have mandated purchase processes. Examples of these include multiple tenders, preferred supplier agreements or interdependence in the form of just-in-time purchasing and delivery. Brand shifting for the consumer may be relatively hard, due to emotional attachments to brands and so forth, and businesses also have difficulties in moving between suppliers, especially where high levels of interdependence and coproduction have arisen. Decisions to increase market share in the B2B marketplace face considerably different strategic requirements from those associated with the same strategy in consumer markets. This will be examined further in later chapters.

Consumer decision process

Belk's (1975) simplified model of consumer behaviour is a four-part overview of the consumer behaviour decision-making process. As the name suggests, this is a simplification of the actual processes that occur within the marketplace, and as such, it represents a stylised view of the world. Belk considered the process leading to a given behaviour to be the influence of the situation, the product (or value offer) and the person, all of which contribute to the final action. Each component is defined as follows:

- *situation*: the external influences on the decision process
- *product*: the marketer's value offer to the consumer
- *person*: the consumers themselves, and their internal mental processes, knowledge, memories, skills and abilities
- *behaviour*: the outcome that was divided into purchase, trial, continued information search and rejection.

Situation expanded

In Belk's simplified model, situation was the most complex of the conditions as it covered every external factor, ranging from weather through to social pressures. The four categories of situation are:

- *communications situation*: the conditions under which the consumer receives the product information
- *purchase situation*: where the consumer makes the purchase, e.g. whether it is bought directly through a retailer, over the counter at a pharmacy or via mail order
- *usage situation*: how and where the product will be consumed, and under what conditions the product will be used
- *disposal situation*: the consideration of how to dispose of the used product.

Whilst the four situation categories tend to impact most heavily on the tactical level of marketing, it is worth assessing their influence on the consumer, and the product choice, at the strategic level during the analysis phases. For example, understanding the product disposal situation can assist in planning market penetration strategies based on expanding the market or increasing the volume of existing sales. Similarly, understanding usage situations will assist in determining if product-use-based niche strategies are viable (e.g. focusing a specific use of the product, such as use of sports energy drinks as mixers for alcohol in nightclubs). Finally, with the increased influence of the stakeholders on the marketing process, understanding the disposal situations for products becomes increasingly important as environmental lobby groups rise in power and legitimacy.

Innovation adoption

Innovation adoption is a critical aspect to understand when dealing with strategies that involve:

- new products (new to the market, new to the company)
- new markets for existing products (new to the market, known to the company)
- significant changes to existing product offerings (changes from the product that was known to both the market and the company).

Failure to understand how the consumer adjusts to innovations can lead to problems with strategies that are dependent on new product sales for growth, or new markets for expansion. Consequently, the focus here needs awareness of the broad categories of innovations, how each of these differs, and the strategic implications that arise from each category.

Types of innovations

There are three types of innovations:

- *really new products (discontinuous innovations)*, which are those types of new products that create markets, define new product categories, cause the consumer

to form new behaviours and are difficult to associate with a single existing product. Innovations that redefine behaviour are relatively rare—even the apparently radical shifts between radio and television could be demonstrated as 'radio with pictures', whereas radio introduced a totally new behaviour pattern of listening to a small box instead of attending a show.

- *quite new products (dynamically continuous innovations)*, which are those types of products that represent a radical shift or upgrade in a product category, but which can be traced to an existing product, behaviour or concept. The notion of the 'horseless carriage' made the car easier to accept. Although automobiles were new, wheeled transport in the form of horse-drawn carriages provided a continuity of behaviour (transportation).
- *continuing product (continuous innovations)*, which are those products where changes have occurred in the features of the product due to advances in technology, improvements in manufacturing, or changes in social attitudes. For example, whilst the first home computer was a quite new product (the merger of a television and a typewriter), the movement from a Pentium III chip to a Pentium IV chip was a continuation of an existing product line (computers) and existing behaviours (computer use), and represented little upheaval in the consumer's behaviour pattern.

The strategic importance of recognising the type of innovation is paramount. Whilst many organisations want to appear to be innovators, the way in which the different groups of consumers deal with innovations varies significantly, and offers strategic advantages and disadvantages. For example, the release of a really new product into a market represents a high-risk strategy where the company has to convince the consumer to radically alter their behaviour, take a social risk at adopting an untried (and possibly unfashionable) product, and pay a price premium for the privilege. In contrast, bringing a continuous innovation product to that market represents the decision to release a variation of an existing product that the consumer is familiar with, understands how to use, and for which the consumer probably has an existing brand preference. Different strategies will also influence what type of innovation the product is—a continuous innovation in one market may become a dynamically continuous or discontinuous innovation in another. The impact of strategy on innovation types will be covered again in Chapter 7–13.

Segmentation, positioning and branding

Segmentation, positioning and branding are the cornerstones of marketing strategy. Each represents both a strategy in and of itself, and includes tactical methods to implement a strategy. In addition, strategies such as product development can make use of segmentation through targeting the innovator segments, branding and positioning through integrated marketing communications.

Segmentation

Segmentation is the method of dividing an existing market by a series of sub-factors such as demography, psychographics, geography and predicted or actual sales figures. The

strategic value of segmentation is to refine the organisational focus on a market that is seen to be profitable, viable and hopefully sustainable. Consequently, reference to segmentation recurs frequently throughout the text, with a heavy emphasis on the technique in the niche marketing strategies (Chapter 12). The key aspects of segmentation to be considered when setting a marketing strategy are:

- Market segments need to be heterogenous (between), and homogeneous (within), that is, each segment must be sufficiently different and identifiable from the broader homogenous market to represent a clear sub-market, but at the same time must be sufficiently internally similar to respond positively to the same marketing strategy.
- The purpose of segmentation is to focus the organisational resources on a narrower band of consumers than the broader market. This should lead to greater capacity to service the market more accurately, meeting specific value needs, and addressing key stakeholders within the segment.
- Bases of segmentation can include:
  — *geographic segmentation*, based on physical location
  — *demographic segmentation*, based on factors such as age, gender and family status
  — *lifestyle or psychographic segmentation*, such as interests, attitudes, religious beliefs and activities, such as sports participation
  — *behavioural segmentation*, including usage rates, propensity to adopt a new product, value proposition sought, loyalty to the firm and user status (purchaser/non-purchaser).
- Optimum segmentation strategies combine more than one basis of segmentation, for example, a geographic segmentation which combines with demographic and behavioural segmentation can identify the size of the market of males in a specific region who purchase the product at least monthly and so forth.

Positioning

Positioning is both a strategic and a tactical decision which, although influenced by the marketer, is ultimately in the control of the consumer. Positioning refers to where the consumer sees the organisation fitting into the marketplace, and which competitors are the closest providers of alternative product offerings. Consequently, positioning is a relative statement, rather than an absolute statement. Further, the product or organisation's actual position, as opposed to its intended or planned position, is determined by the consumer. The organisation can consciously pursue a positioning strategy decision to sway the view of the consumer, however ultimately it is the consumer who determines the product's perceived position. Positioning will be a recurring theme of Chapters 4–6, as it combines external perceptions (external analysis, Chapter 5) and the internal selection of competitive advantage (internal analysis, Chapter 4), along with the strategic choice to pursue a deliberate market position (strategic objectives, Chapter 6). In summary, selecting and acting on a positioning strategy requires:

- the identification of a possible set of competitive advantages
- the selection of the appropriate or optimum advantage
- the effective communication of this advantage to the market
- the delivery of the value proposition to the consumer based on this position.

For example, an airline may regard its competitive advantages as being low cost, relaxing environment, and friendly service. It then selects friendly service as a positioning statement, promotes this message to the market—'Fly the friendly skies'—and attempts to deliver this position by hiring personable staff. Having established a position based on friendly service standards, the organisation can make use of a brand leadership strategy ahead of a cost leadership strategy. Similarly, an organisation positioned on innovation, such as 3M, will emphasise this position through product development strategies.

Conclusion

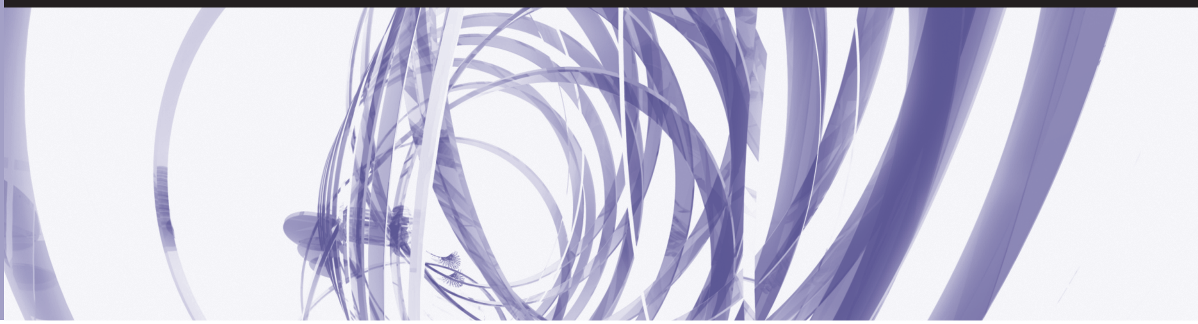
One of the characteristics of marketing, which makes it such an interesting area of study and work, is the fact that it is a living and applied discipline. The downside of this is that it is constantly evolving in light of changing business practices and business model innovations. This is most clearly seen in the evolving definition of what 'marketing' is—and, flowing on from this, what its role within the organisation and society is and should be.

The practice of marketing is in a state of constant evolution. As practices emerge, they are formalised and conceptualised into new models of marketing. Some of the most important advances in the marketing theory and practice to emerge between the different definitions of marketing of 1985 and 2004 is the concept of the lifetime value of the customer and the need for organisations to consider the importance of investing in developing and maintaining relationships with their clients for long-term organisational success.

Despite these conceptual advances, there are some core activities and ideas that remain constant and essential to the study and practice of marketing. Critical to developing quality marketing strategies is a thorough understanding, and effective implementation, of market segmentation and positioning. The purpose of this chapter was to give an overview of these core concepts and highlight the key trends in marketing theory and practice. Chapter 2 follows this theme and provides a review of the key strategic models used to underpin the development of marketing strategy.

Review of key strategic models

CHAPTER 2



Introduction

Chapter 2 is a review of a selection of common strategic models and decision-making tools including an overview of classic models such as Ansoff's Growth Matrix, Porter's Five Forces and the product life cycle.

Chess strategy v. marketing strategy

Chess is one of the oldest strategy games in common use today, and it holds significant sway over much of the thinking regarding strategy. Unlike business strategies, all strategy in chess is conducted within a mathematically finite arena. There are only a limited number of positions possible within the confines of the board and the available pieces, even if there are 71 852 possible positions after four moves alone. Simply having a limited board space of 8×8 squares and 32 pieces means that it is mathematically possible to calculate the number of possible alternative outcomes, which is approximately 10^{120} moves.

Although 71 852 possible positions exist after four moves, there is a more limited number of useful opening plays which have been developed over time. Chess moves can be refined down to the point that it is possible, although unlikely, for the white pieces to

be able to force a checkmate within 16 moves. Although the chess game consists of a range of choices well beyond the processing power of most humans, strategic set plays have been developed to produce optimum results, based on the preconditions of the chessboard.

Business strategies do not operate within the confinement of the chessboard, and as such, exist in universes where there are far more than 10^{120} moves available in the whole market. However, much like chess, there is a range of optimum set plays that have been observed and developed over time. Whilst business models are not at the point of a 16-move checkmate scenario, they do represent the narrowing of the possible moves from 71 852 choices to a reasonable number of alternatives based on the conditions of the market (board). In addition, the business models presented in this chapter are steps in the process, rather than maps to the endgame. As each model is followed, or strategies implemented based on these pre-determined moves, they will most likely trigger reactions from consumers and competitors alike. Consequently, use of these models is an ongoing process—like a good move set in chess, or a rehearsed move on the sports field, they are no guarantee of success, but instead are a method of improving the odds based on the conditions of the market and the past experiences of other businesses.

Common models

In marketing theory and practice, there is a range of models which have, for various reasons, reached a high level of recognition and repetition in the business sector. Periodically, the validity of these models is called into question, and attempts are made to scientifically prove or disprove their applicability to the business sector. However, this approach treats the model as a form of recipe, where following the instructions can (and should) result in the same outcome each time. In reality, and with the complexity of market dynamics, these models should be seen as guidelines rather than hard and fast rules. In every case, the model needs to be adapted and adjusted to the specific conditions of the market, the firm, the competitor and the environments for it to be valuable. For example, applying the same model to international airline travel and the domestic childcare market without adaptation does not make business sense. Similarly, rigid interpretation of the models without regard for the specific environment is also missing the point—the chess player who does not adapt their move set according to their opponent's actions is going to fare badly. The same approach applies for any business—adjusting, adapting and applying the models to the context to assist in the decision making should improve outcomes, but can never guarantee them. The following sections examine a set of common models used for strategic planning purposes, including:

- Porter's Five Forces
- Porter's Generic Competitive Strategies
- the Boston Consulting Group (BCG) Growth Share Matrix, which is used for portfolio balancing and planning

- the General Electric (GE)/McKinsey Directional Policy Matrix Variant, which, like the BCG Matrix, is a tool for portfolio planning
- Ansoff's Growth Matrix.

These models are outlined briefly in this section, and dealt with again in greater depth in Part 3 of the book. At this stage, the purpose of overviewing the models is to demonstrate the context for each model, before examining the specifics of applying them to strategy development.

Porter's Five Forces

Porter's (1979) model of five industry-shaping forces has had a chequered past. Whilst intuitively appealing, and a mainstay of strategic marketing writing over the years, the model has often been misunderstood to represent a set of hypotheses to be statistically examined in a controlled environment. Porter didn't present the model as a structural equation model with a fixed percentage success rate, and as such, it should not be a surprise when the interpretation of these ideas into equations leads to their failure. The Five Forces Model is a set of ideas to consider, and accept or reject as appropriate for the organisational situation. The five forces are:

- *rivalry amongst competitors*—that is, the extent of competitiveness between existing players in the market. Competitiveness can be a dual-edged phenomenon—low levels of competition in a market may indicate collusion and high levels may indicate a vibrant market with limited brand loyalty amongst the customers. The shaping effect of competitive rivalry is to ask how the level of rivalry will influence the organisation, and how the rivalry will determine reaction to the organisation's marketing strategy. For example, the competitive rivalry between Microsoft, Sony and Nintendo in the video game console market triggers price battles, and aggressive responses to each other's actions. In contrast, the DVD marketplace, which also features Sony and, to lesser extent, Microsoft, has less competitive rivalry between the manufacturers who are all cooperating to introduce the BluRay DVD format.
- *threat of new competitors and market entry*, which is where markets become sufficiently profitable to attract new entrants. The arrival of new competitors can drive prices down as existing players attempt to thwart price competition by the newcomer, which is often the approach taken by larger organisations (e.g. QANTAS) to fend off smaller start-ups (e.g. Virgin Blue). Alternatively, competitors can come from above and below as suppliers of parts may attempt to move down into the market (e.g. manufacturers selling directly to the end customer, as do Dell), or retailers may move upwards by producing their own home branded products (Woolworths Home Brand).
- *threat of substitute products*, where a market need can be met by an alternative product. The current most high profile example of the danger of substitute products has come from the film industry, which has lost considerable market share to alternative entertainment formats such as video games, cable television and DVD

rental. Similarly, the market for audio CDs is threatened by the popularity of the iPod, and capacity to buy music from iTunes without needing to purchase a physical CD.

- *bargaining power of the suppliers*, where the supplies needed for business are controlled by a limited number of providers. For example, in the IT sector, the limited number of RAM manufacturers means that fluctuations in their output levels will impact on the price of computers and the profitability of the manufacturers relying on these parts. Similarly, Microsoft has a greater bargaining power in the computer market, where it is one of the few providers of operating systems and office software, than in the video games market, where they are one of many providers.
- *bargaining power of the buyers/customers*. Where the market is small, or there is a dominant buyer (e.g. business to business sales), little power is held by the seller—in the case of markets based around servicing one or two large clients, those clients can exert considerable influence.

Porter (1979) also identified that these five forces were interconnected, insofar as the competitiveness of the marketplace was influenced by the power of the supplier, customer, and the threat of new player, or as alternative products influenced market decisions. Similarly, the power of the customer is weaker where limited alternatives exist and there is a strong supplier. For example, QANTAS and Virgin Blue have little competition against them in the long-distance travel market, with substitute products such as driving, bus or train travel not being effective alternatives. Consequently, the customer has reduced bargaining power against the air travel providers, however, due to competition between the two suppliers, the bargaining power of the customer is increased. Should the level of competitiveness between the airlines reduce, the power of the customer will also decline. Ruocco and Proctor (1994) illustrated the interaction of the five forces, based on Porter's proposition that the competitiveness of the market is subject to the influence of the other four forces (Figure 2.1).

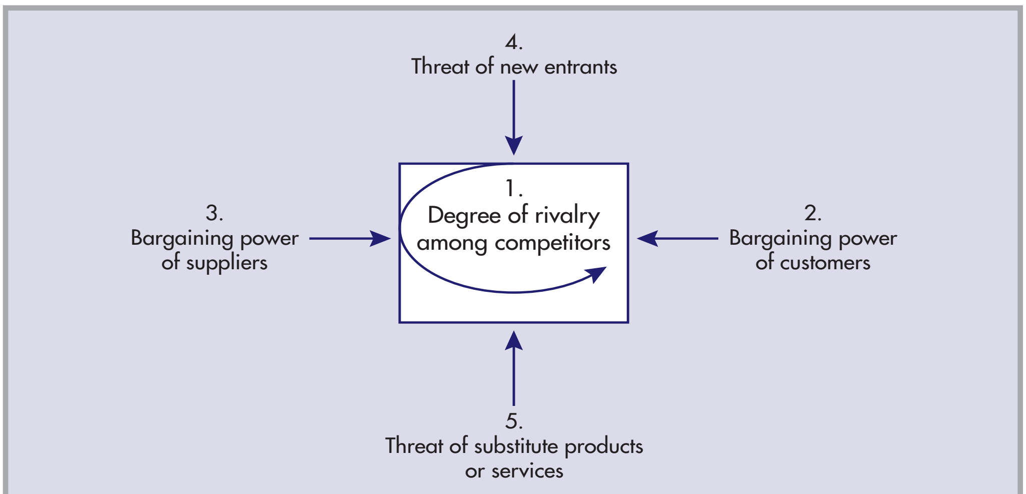


FIGURE 2.1 **Porter's Model of Competitive Forces**

Source: Ruocco, P & Proctor, T 1994, 'Strategic Planning in Practice: A Creative Approach', *Marketing Intelligence & Planning*, Vol. 12, No. 9, p. 27. Reprinted by permission of The Free Press.

Porter later introduced additional factors to the core five forces, based on various marketplace conditions. For example, some sectors are more heavily influenced by government, in which case government regulation would provide a sixth influence. Porter does not see the initial five as the definitive list of forces that drive competition. The Five Forces Model will be examined again in Chapter 5, External analysis, where it is used in part as an analytical tool in information gathering processes required for determining the organisational strategy.

Making use of the Five Forces Model for strategic marketing

The Five Forces Model has greatest value in strategic marketing in the external analysis of the firm, as it provides a framework for testing the position of the firm in the marketplace. Although this is covered in depth later, the basic value of the forces model is that it encourages the marketer to think through the questions listed in Table 2.1.

Answering the question of competitiveness will influence product and pricing decisions, and may impact on distribution options as new competitors may force the organisation to retail in different outlets. For example, music retail stores had dominated the distribution of CDs, however the advent of in-car CD players made the petrol station a viable distribution alternative for CDs, thus opening up the marketplace. Similarly, legitimate paid downloads

TABLE 2.1 Strategic questions arising from the Five Forces Model

Questions	Sub-components to consider
How competitive is the marketplace?	What are the competitive conditions that the firm is facing, (e.g. is there potential for market growth)? Are products mostly undifferentiated or are there opportunities for specialist products?
Is this a closed or open marketplace?	What is the realistic likelihood of new competitors entering the market? What entry barriers exist, and can those barriers be influenced by the firm's activities?
Who holds the power in the relationship between the firm and the suppliers?	Does the supplier currently hold the power? Does the customer currently hold the power? What conditions are required for the power to shift?
What sort of substitute products can the customer use to meet the need that the firm's product is currently meeting?	What is the core need that is being meet?

of mp3s opened the music marketplace to include the internet as both a marketplace and distribution channel. Control of the market will determine, in part, the amount of bargaining power held by the suppliers, and the manoeuvrability of the firm in being able to meet spikes in demand. For example, where a single manufacturer supplies a high-demand product (e.g. Apple and the iPod product line), the supplier determines the allocation of product to the retailing firm. However, where a wider range of product suppliers exist, the retailer determines what product gets carried or not carried. Supermarket chains can charge for shelf space due to the large number of products being placed inside the limited shelf space. In contrast, attempting to charge Apple a premium to carry the iPod is unlikely to succeed.

Understanding the dynamics of the market is critical in determining who currently holds the power in the relationship between the customer and the firm. Whilst marketing is the management of the relationship between the customer and the firm, for the benefit of the firm and the stakeholders, the power dynamic in the relationship is fluid. Power is based on the demand for the product (high demand shifts power to the provider), the size of the customer (large customers have more power), and the range of alternative providers in the market (limited competition reduces consumer power). In addition, the definition of marketing requires an additional element to be added to the Five Forces Model—the influence of stakeholders. Whilst the Five Forces Model is focused at the business level, the role of the stakeholder now has an impact directly on marketing, and indirectly on business orientation.

The final question is the anti-marketing myopia approach that focuses on customer needs rather than the company's product offering. If the customer need is for entertainment, then substitute products can come from a wide range of sources—games, movies, tourism, books, shopping experiences, sport, or time spent with friends. In contrast, a book company looking at substitute products at the product offering level will only see rival book products, and miss a possible market threat from DVDs, video games or customers shifting to reading online.

Porter's Generic Competitive Strategies

Porter's Generic Competitive Strategies model was developed in parallel to the Five Forces Model, and as such, is best used as a mechanism for translating the information derived from the Five Forces Model (e.g. level of competitiveness of the market) into one of three possible approaches for creating a sustainable advantage. Porter (1980) believed that an organisation could use its capacity and the conditions of the market to gain a superiority from one of three approaches:

- *cost leadership*, which relies on being the company that provides products at the lowest feasible cost (Chapter 10). For example, if it costs United Pictures $100 million to produce a box office #1 film, and New Line Cinema can produce a similarly ranked film for $80 million, then New Line will gain a competitive advantage from the $20 million difference.

- *product differentiation*, which depends on finding a unique product offering and making this specific product offering profitable, sustainable, and something the consumer desires (Chapter 11). For example, Toyota has developed the Prius hybrid electric motor and petroleum fuel based car that is differentiated from petrol-only alternatives.
- *niche marketing*, which relies on finding a market niche, and dominating it in a particular market segment (Chapter 12). Niche markets involve servicing narrow market needs, such as the Wolf Claw II specialist video gaming keyboard by Pd Scientific Products <www.pdscientific.com.sg/>. Niches need to be profitable, sustainable and well targeted, but as the WolfClaw product demonstrates, they do not need to necessarily be able to be sold to a wider market.

Differentiation and niche represent separate levels of market focus. Differentiation is industry wide, based on factors such as branding, quality or innovativeness, along with meeting a specific need in the market. Niche strategies require a focus on a specific market segment, and producing a product for that niche in a way that primarily appeals to the customers in that small group. It can include niche-based cost leadership or niche-based product differentiation as the approach to niche management.

The value of Porter's Generic Strategies

Porter's generic marketing strategies provide the groundwork for business decisions in much the same way that a set play in chess provides the groundwork for capturing an opponent's piece. The generic strategies, which are addressed in depth later in the book, each rely on certain market preconditions. Where these conditions are met, Porter's suggested options give the marketing strategist a starting point to consider their optimal strategy. For example, niche marketing requires the preconditions of existing market research, market segmentation, and a small, but viable, known market to target with the niche strategy. Similarly, cost leadership requires economies of scale, labour efficiencies, improvements and refinements in the production process, and long-term low-cost suppliers of materials or products. Although the existence of the preconditions does not bind the marketer to one of Porter's strategies, these strategies are good starting points for the organisation to consider its specific business plans.

BCG Growth Share Matrix

The Boston Consulting Group Growth Share Matrix was developed as a method of examining the strategic direction of products, product portfolios and value offerings to the consumer (Figure 2.2).

In essence, it consists of a two by two matrix of relative market share and predicted market growth, which creates four possible types of product:

- *stars*, which are high growth and high market share. The stars are profitable, but also require high levels of resource investments to manage and maintain the

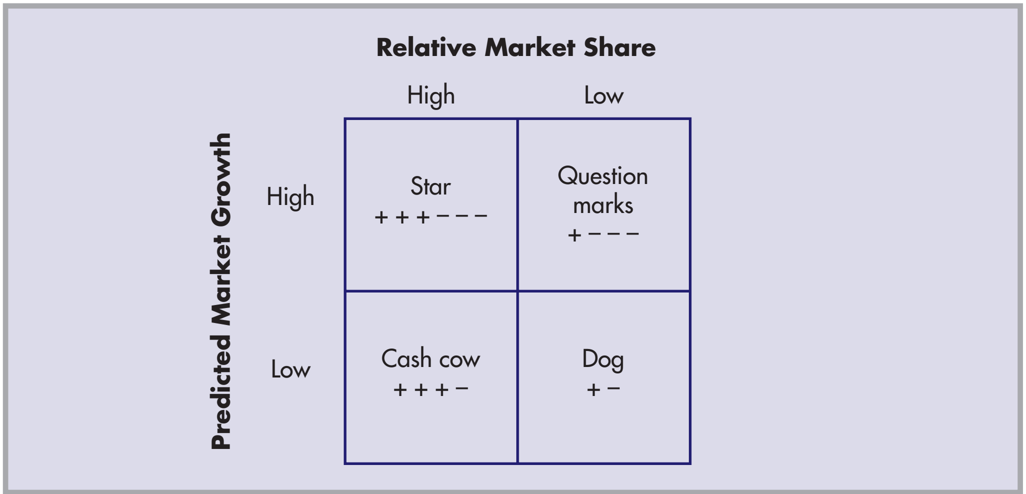


FIGURE 2.2 **The BCG Matrix**

Source: Peters, J 1993, 'On product and service management', *Management Decision*; Vol. 31, No. 6; p. 50. Republished with permission, Emerald Group Publishing Limited.

growth. Products in the 'star' category are in a developmental position where the aim is to gain, and hold, market share until the market matures and the stars turn into cash cows.

- *question marks*, which are the high growth markets with low market share. Question marks are risky areas where additional investment of time, organisational effort and money can either move the product into the star category, or be a waste of resources and turn into a cash-trap or 'dog'.
- *cash cows* represent a large slice of an established and profitable market. Although the cash cow has low growth, this is regarded as a positive feature, as it represents the maturity of the product and the market. Products in these categories sustain the organisation's capacity to operate, and often cross-fund the investment in stars (replacement cash cows of the future), or cover the costs of speculative investment in the question marks.
- *dogs*, which are the poor performers that are low growth, low market share and require considerable resources of management time, usually in excess of what they are worth to the firm. These products are usually dropped from the firm's portfolio. However, companies may retain the 'dogs' for alternative reasons, such as community service obligations where the company continues to service an unprofitable area (cross-funded by a cash cow) to achieve social objectives.

Criticism of the model

The BCG Matrix is powerful but also simplistic. The use of a two-column matrix of 'predicted market growth' versus 'relative market share' does not fully assess the implications of a market. For example, whilst a market may have high growth, and the company may hold a

small share of the market (question mark), that share may be less sustainable than a dog (low share, low growth) in another market, simply based on the size of the two markets, and the investment required to exploit the market.

The BCG Matrix is also based on several assumptions, that:

- *the business units operate independently*. A cash cow (recordable DVDs) may only continue being a cash cow because of the presence of a dog (DVD recorder), and this is not captured within the BCG Matrix. Similarly, the matrix assumes that a poor performing product (dog) should be discarded, when it may be needed to block a competitor entering the market.
- *market attractiveness is measured in terms of growth and market share*. Whilst growth is useful as a measure, other factors—such as entry barriers, capital requirements, sustainability, competitiveness, substitute products and number of other competitors—can make high growth markets less valuable than lower growth, but less crowded alternatives. For example, a high volume market with low growth (e.g. DVD sales) may produce a larger financial return than a niche market with rapid growth, but small size (e.g. movies for mobile phones).
- *market share is being defined consistently*. Does the organisation define the share of the market as being the share of a specific market niche? Or the broader marketplace? Or the whole of an industry? A company making a profitable niche product in specialist winter sports (snowboarding) gear may occupy 60% of their specialist niche. However, in the broader marketplace, that 60% niche may only translate to 5% of the snow-based winter sports market (skiing, snowboarding, sledding). When considering the whole of the winter sports industry, including rugby league, rugby union, AFL, soccer and other snow sports, that profitable 60% niche may be less than 1% of the overall market. Consequently, defining market share has a major impact on whether the product may be a dog, cow or star.

Composite Portfolio Model: the Directional Policy Variant

The GE/McKinsey Matrix is a composite portfolio model that expands the basic premise of the BCG Matrix. The GE/McKinsey Matrix consists of two measures:

- *industry attractiveness*, which is every factor that can influence the profitability or sustainability of a market, as perceived by the organisation
- *the business's competitive position*, which is the business's internal analysis of its capacity to deliver the value proposition to the consumer, capacity to manufacture or provide the product/service offering, and relative strengths in the market (e.g. cash flow, venture funding).

These two factors are used as the axes of the matrix, and are divided into three categories ('high', 'medium' and 'low') to correspond with the assessment of the firm and the market (Figure 2.3).

Industry attractiveness

Business strength	Low	Medium	High
Low	Direct (red)	Niche (red)	Invest with care (amber)
Medium	Divest or harvest (red)	Monitor (amber)	Build share (green)
High	Harvest (amber)	Defend share (green)	Deploy best resources (green)

Note:
Red = Stop   Amber = Proceed with care   Green = Go

FIGURE 2.3 **The GE/McKinsey Matrix**

Source: Peters, J 1993, 'On product and service management', *Management Decision*, Vol. 31, No. 6; p. 50. Republished with permission, Emerald Group Publishing Limited.

The GE/McKinsey Matrix produces three possible strategies from the nine possible outcomes of the assessment of industry attractiveness and business strength.

- *Green*, where there is a high strength/high attractiveness, medium strength/high attractiveness, high strength/medium attractiveness match. The investment strategy is based on either maintaining a beneficial position (high strength/high attractiveness, or high strength/medium attractiveness) or improving to an optimum position (medium strength/high attractiveness). These products were either stars or question marks in the BCG Matrix, depending on their share of the market.
- *Amber*: selective management, which is the middle of the road option where the company is dominant in a weak market (high strength/low attractiveness), middle ground (medium strength/medium attractiveness) or with limited capacity to work in a profitable market (low strength/high attractiveness). These strategies assume profitable income, and represent the 'cash cows' of the BCG Matrix. In addition, the amber signal indicates that caution should be used before proceeding—in this traffic light metaphor, it can go from amber to green or red. Real traffic lights tend just towards red.
- *Red*, which is divest or harvest time, implementation of defensive strategies and the point at which to decide whether or not to continue in the marketing. These sections are usually associated with the 'dogs' of the BCG Matrix (that is, low

strength/medium attractiveness, low strength/low attractiveness, medium strength/low attractiveness). Divesting requires the organisation to produce an exit strategy to leave the market, whereas harvesting is a staged withdrawal that relies on maintaining a reduced position in the market all the time the market remains profitable, but with the ultimate aim of divesting the 'dog'.

The GE/McKinsey Matrix and the BCG Matrix are both based on a similar thematic approach of matching strength against opportunity to determine possible strategies. In these two models, the approaches have been limited to three to four response types, which may not suit a wide range of markets. However, as basic framework, these models can be expanded into offering more complex alternative strategies.

The Directional Policy Matrix Variant

The GE/McKinsey Matrix has seen several variations developed for specific organisational environments. One of the more enduring variations, and the chosen strategy matrix for this text is the Shell Chemical Directional Policy Matrix (figure 2.4) (Robinson, Hichen and Wade, 1978). This variation on the GE/McKinsey Matrix emphasises a multivariate measure of market attractiveness and business strength.

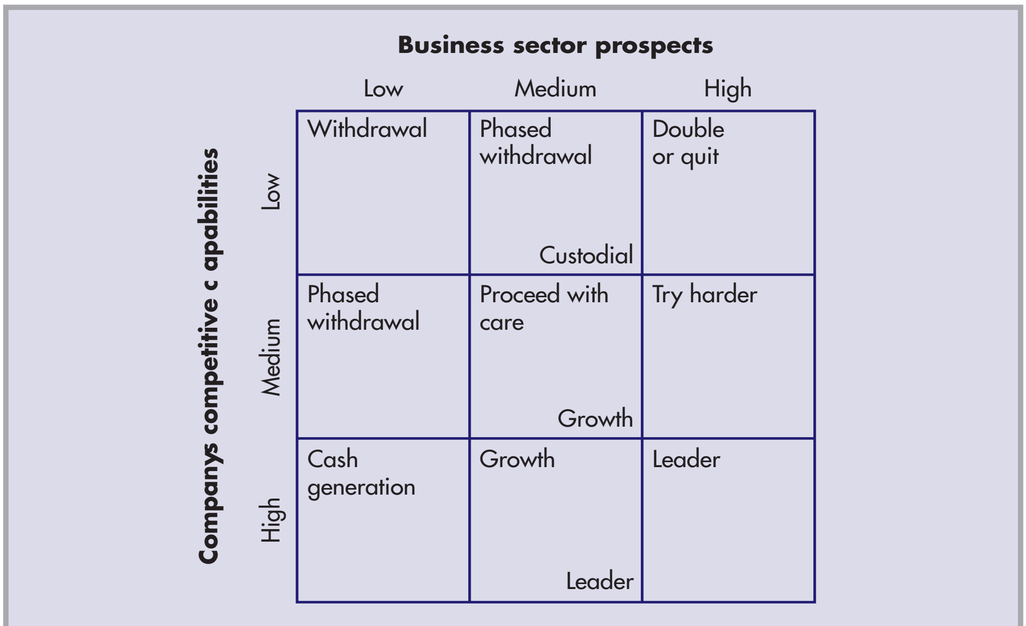


FIGURE 2.4 **Shell Chemical Directional Policy Matrix**
Robinson, S. J. Q., Hichen, R. E. and Wade, D. P., (1978), 'The Directional Policy Matrix,Tool for Strategic Planning', *Long Range Planning*, 11 (June), pp. 8–15. Reprinted with permission from Elsevier.

The result is nine alternative strategies, which Hussey (1978) defined as:

1. Leader (high competitive position/high industry attractiveness), which is the peak point in the operation of a business—being the leader in a highly attractive market. All

strategies in this field are based around defending and holding this position for as long as possible, and cross-funding ventures in the Growth leader and Try harder categories.

2. Growth leader (high competitive position/medium industry attractiveness), which corresponds to the BCG Matrix question marks in situations where growth is good and the organisation has the capacity to improve to capitalise on the opportunities presented in the marketplace. Growth leaders have the capacity to be turned into Leader category products.
3. Try harder (medium competitive position/high industry attractiveness), which is where the market conditions are extremely positive, but the company has not sufficiently developed to take advantage of that fact. Low competitiveness in an attractive market can be redressed through investment of time, resources and organisational capacity.
4. Cash generation (high competitive position/low industry attractiveness), which is the cash cow of the BCG Matrix. It is where the company holds a solid market share in a viable and financially attractive marketplace.
5. Proceed with care (medium competitive position/medium industry attractiveness), which is where the market and the company are both at a middle point where the company is neither dominant or clearly deficient, and the market is neither highly attractive or clearly worth leaving.
6. Double or quit (low competitive position/high industry attractiveness) is the point where the organisation has to either invest heavily in its competitive capacity, or withdraw from the market. Whilst the opportunity is present, an organisation in this position currently lacks the ability to capitalise. Although the 'obvious' strategy is to invest heavily, the sustainability of the market needs to be considered to avoid converting a low competitive position in an attractive market into a strong position in a less attractive market.
7. Phased withdrawal 1 (medium competitive position/low industry attractiveness) is where the company occupies a reasonable position in an industry that lacks profitability. Although the position is strong, the resources should be examined to determine if they could be better used elsewhere in the organisation.
8. Phased withdrawal 2 (low competitive position/medium industry attractiveness) is where the industry is reasonably profitable, but the organisation lacks the capacity to capitalise on the market opportunities. The organisation has the option of either withdrawing from the market (writing off the failed venture to tax and experience) or trying to improve its competitive position, assuming that the resources could not be better used elsewhere in the firm.
9. Withdrawal (low competitive position/low industry attractiveness), which is where the firm is losing money on a product and has low market share and low capacity to improve the position.

Strategic value of the BCG and GE/McKinsey models

One feature of the matrix models which is paradoxically both a criticism and a valuable benefit is that, in many respects, they state the obvious (e.g. a company with strengths in a

good market will want to retain the strength and retain the market share). However, beyond the initial sense that the model says little that isn't commonsense is the realisation that both models show ideals of market conditions, and provide decision-making frameworks based on those ideals. The GE/McKinsey model, along with Shell Chemical's modifications, has produced nine starting positions for a strategic analysis. For example, where the organisation has a product in the 'Try harder' square, the matrix model shows the possible progressions based on successful adjustments to the competitive position (either Leader or Growth leader), or the negative effects of a downturn in the attractiveness of the market (Phased withdrawal) or successful upgrade of the business and downgrade of the market (Proceed with care).

By visualising possible outcomes, it becomes easier to look at the broader strategic implications of a decision to improve the business competitive position, or seek a more attractive market. Ultimately though, the real value of a model such as the Shell Chemical variant of the GE/McKinsey model is that it assists the marketing strategist to consider the implications of each square, and to assess the strength of the business against the value of the potential market. Placing the emphasis on the business analysis (Chapter 4 and 5) required to make use of a policy matrix will return greater rewards than simply locating a starting position on a 3 × 3 grid and applying a generic strategy out of the box.

Ansoff's Growth Matrix

Whilst the GE/McKinsey and Directional Policy matrixes offer a range of alternative market positions, they offer limited directional advice. In contrast, Ansoff's Growth Matrix is a model designed to assist in selecting one of four growth strategies, based on the existing or new markets and existing or new products (Figure 2.5).

	Existing products	New products
Existing markets	Market penetration	Product development
New markets	Market development	Diversification

FIGURE 2.5 **Ansoff's Growth Matrix**

Source: Watts, G Cope, J & Hulme, M 1998, 'Ansoff's Matrix, pain and gain: Growth strategies and adaptive learning among small food producers', *International Journal of Entrepreneurial Behaviour and Research*, 4(2), pp. 101–11.

Ansoff's 2 × 2 matrix produces four possible strategies, which are:

- *market penetration* (existing products, existing markets), where the organisation attempts to increase sales of existing products in existing markets (Chapter 7). This is done through repeat purchase, increasing the volume of use, and/or finding new uses for the existing product. For example, something as simple as altering the instructions on shampoo from 'wash twice per week' to 'wash daily' to 'use twice daily' can increase the volume of sales of the product of the existing product to an existing market.
- *market development* (existing products, new markets) is where the organisation looks for a new market for its existing product range (Chapter 8). This can be through market segmentation, non-users being targeted to become users, adding additional distribution channels such as moving from specialty stores to supermarkets or geographic development such as taking a regional product to a national or international market. For example, an organic muesli product can use a market development strategy based on distribution to expand sales by selling into supermarkets as well as health food stores.
- *product development* (new products, existing markets), where the organisation brings new products to its existing markets by adding new features, improving alternative options and developing entirely new options (Chapter 9). For example, Apple has provided a range of new iPod products to its existing iPod markets, for example by removing the screen and play list functions from the original iPod and releasing it as the iPod Shuffle.
- *diversification* (new products, new markets), where the organisation takes a new product to a new market. This is the case with any discontinuous innovation, or any entrepreneurial start-up company. Diversification strategies can arise from a variety of sources from internal organisational innovation, to acquisitions of smaller firms, or expanding a brand name from one product category (e.g. LG white goods) into a new category (LG mobile phones). Sony has had one of the most high profile diversification strategies, moving from electronics manufacturing into areas such as music, movies, online games and other entertainment systems.

Strategic impact of Ansoff's Growth Matrix

Ansoff's Growth Matrix has an inherent assumption of growth as it was designed as a mechanism to be used when considering growth alternatives as a result of earlier strategic decisions. One recurring misconception in business strategy and business planning is the idea of mandatory growth as a signifier of business success or baseline business health. Perpetual growth, like perpetual motion, is an unrealistic goal for business. Consequently, the Ansoff Growth Matrix should only be used when the firm has set a growth strategy based on market conditions and organisation strengths and capacities.

Market Conditions Model: product life cycle

Whilst the previous models have been strategically focused, the product life cycle is a conceptual diagnostic tool. The purpose of the model is to map the rise, and fall, of the sales of a product over time. In short, the model demonstrates the movement of a product through six different ideal 'life cycle' phases:

- *introduction*: where the market first encounters the product, innovators adopt it, profits are low, prices are high and cost recovery is the primary motive of the marketing and accounting departments
- *early growth*: where the early adopters, opinion and fashion leaders adopt the product
- *growth*: where the broader market of early majority purchases the product, competition increases, and the market leaders are occupying position one in the GE/McKinsey Directional Policy Matrix Variant (the GE Matrix)
- *late growth*: products are repurchased, secondary uses are found for the product, or additional copies of the product are used (e.g. one DVD player for the living room, one for the bedroom). Late growth also ties into the late majority adopter category who are belatedly joining the fashion cycle
- *maturity*: the market has stabilised, product variations are widespread, and the market is saturated with product offerings
- *decline*: the final phase where the product is either retired, recycled into the maturity phase or divested. This part of the model best reflects categories 7, 8 and 9 from the GE Matrix.

Although the model is presented as a mathematical model, it is a conceptual model of an ideal world where a product makes a smooth progression from introduction through a sequential process to be gracefully retired in the decline phase. In reality, products may fail to make it beyond introduction before nose-diving straight into decline, or a complex product may be introduced and reintroduced to the market several times before progressing into anything that resembles the criteria of the early growth phase of the model. The model is an important part of processing the potential scenarios for the organisation's product—for example, is a new product still in introduction or early growth? If so, then the strategic decisions will focus more on growth strategies to move it forward into the market. In contrast, a product that appears to be in the decline phase of the curve requires a different set of strategies. This is a diagnostic tool to assist and inform the marketer rather than a prescriptive device that will set strategies or marketing tactics.

Variations on the product life cycle model

There are numerous variations on the basic product life cycle theme. At the core, each represents a type of sales pattern over time, whether it be a high peak, followed by consistent sales, or a series of peaks and troughs. Kotler and Keller (2006) outline six types of product life cycle curves, each based on specific descriptive criteria.

- *Growth slump maturity* is a cycle based on fast initial sales which peak as the new product becomes the 'must-have' item. Sales then decline to a static maintenance level supported by steady sales to late adopters, and sales to early adopters who are replacing worn out products. Most forms of aggressively new clothing fashions (straight ties, wide lapels) fall into this category.
- *Cycle–recycle pattern* occurs when the product is aggressively sold and pushed in the first instance creating the first sales peak. As sales decline, secondary and subsequent sales campaigns push the peak back up to a level below the first cycle. This produces the semi-sine wave style curve of the cycle–recycle pattern, which is often seen in entertainment products such as video games consoles where an intensive campaign is used to drive initial sales, followed by a secondary campaign to raise flagging sales. This is a routine pattern for promoting a film where the first peak is the box office sales, and the second peak is aimed at the home DVD rental market, and a third spike targeting the home DVD sale.
- *Scalloped pattern* is where the product follows through a sequence of product life cycles as new uses are found for the product, new features emerge, or new users adopt the product. The pattern features total growth in the overall sales figure over a series of smaller, sharper curves rather than a long continuous growth.
- *Style pattern* represents the 'basic and distinctive modes of expression in fields of human endeavour' that are concurrent across a product category (e.g. abstract, surrealistic, realism in art and design). Styles fade in and out of contemporary use, and as such, have longer sine-wave style oscillating curves. This includes architectural designs, political movements and whether the kitchen fridge should have a rectangular or rounded profile.
- *Fashion pattern*, which is a subset of style, represents a faster, four-part curve based on distinctiveness (innovation/introduction), emulation (early growth, early adopters), mass fashion (early and late majority, growth and maturity) and decline (laggards and decline). Fashions are complicated by their variable speeds, as some fashions will satisfy deeper needs and last longer, whereas others will last until too many other people adopt 'the look'.
- *Fad pattern* is a fast-burn product life cycle where a product or idea is adopted quickly, peaks early, and is dropped as quickly as it was adopted. Fads have the shortest life cycle of all categories, as they tend to satisfy a need for novelty, and once satisfying that need, they are no longer novelties and are discarded in favour of the next new object. Pet rocks, this season's 'must have' toy, the 'it' band of the moment—the $2 discard bins of major retailers usually provide a good case study of failed and passed fads.

Criticisms of the product life cycle model

Understandably, there are many critics of the product life cycle (PLC) model. In fairness, the model does have several limiting factors and weaknesses including:

- *lack of clearly defined concepts*, which is evident in the lack of common standards for the application of the model. The PLC can be applied to industries, products, needs, demand, technology and a host of other concepts. Although problematic, the lack of definitions is also a factor inherent in the fact that the product life cycle is a conceptual model of the movement of an object through a community over time.
- *no consistent curve shape*, which is the business statistical equivalent of the product disclaimer 'your mileage may vary'. In essence, since the model is a conceptual description of how products move through a marketplace, the lack of consistent curve shape is understandable.
- *lack of predictive component* is the absence of clear indicators of where and when a product reaches each part of the model. For example, there are no consistent benchmarks to determine if a product is in growth, early growth or even maturity.
- *unclear implications*: a criticism levelled at the practical application of the model, given the lack of advice to guide what specific action should be taken in each stage of the PLC.
- *product bias*, which is the curious complaint that the product life cycle focuses on the product, rather than the customer. In essence, the complaint is that product life cycle based strategies do not place sufficient emphasis on the needs of the market and instead focus on a product orientation.
- *not exogenous*, which is to say that the product life cycle model is also influenced by internal factors that may be unrelated to the marketplace. For example, a strategy meeting that determines a product is approaching the decline phase may expedite the exit strategy, thus ensuring the decline of the product. The market still may have a need for the product but the strategic vision of the company may have determined that the product was in decline, even with pre-existing demand.

The limitations of the model also mean that the misuse of the device will cause problems for the marketer—for example, mistakenly assuming that the analytical and diagnostic nature of the product life cycle can be used as a predictor of future strategy will create problems. Working with the strengths of the model (diagnostic) and not relying on its weakness (not predictive) should see it provide value in the analysis phases that lead in to the creation and selection of strategy.

Impact of the product life cycle

The product life cycle has been criticised to the point where certain authors believe it is no longer a relevant part of business, despite spending a few pages of a book explaining and criticising the concept (Proctor 2000). Given that the purpose of the models covered in this chapter is to act as a guideline for reviewing the state of the business, the PLC remains a useful model, if used correctly. As with other models, the PLC is valuable if used, along with other models, for assessing where the company stands, and what strategy should be adopted to move forward.

The greatest value of the PLC is to consider where a product could be located on a life cycle curve—is it introduction, growth or decline? Then, having worked out roughly where the product sits on the curve, what type of product life cycle curve is desired? A scalloping pattern of recurring marketing campaigns to restart flagging sales? A smooth curve of introduction, adoption then divesting or deletion of the product? Is the product more suited to a hit-and-run strategy with a fad style PLC or could this be managed as a fashion or trend? In general, the PLC's role is to provide a framework for considering where a product has been (growth, decline, flat line) and where it can progress (growth, decline, maturity).

The value of marketing models

A good understanding of marketing models is equivalent to a good practice session for a sports team. Business is a difficult field where there are few opportunities for practice sessions, 'friendly' matches, and simulations. Consequently, a large part of the value of the business models presented here comes from the ability to use these models as a form of mental practice session. Models such as Porter's (1979) Five Forces are not meant as definitive descriptions of reality, but rather, areas to consider when planning a strategy. For example, whilst Porter specifies five forces, there are more forces in existence that influence the success or failure of the organisation. This doesn't mean that the Porter model should be discarded, it just means that Porter's model shouldn't be seen as the end, but rather as an ongoing part of the process of planning.

Using models in practice

Throughout the previous section, the discussion of each model has indicated that it cannot be viewed in isolation, and instead, must be seen as part of a system or whole. Li (2000) explored the development of a hybrid intelligent system, a computer assisted process of addressing problem solving, that used Porter's Five Forces, SWOT analysis and the subjective judgement of individual managers to create an information flow that was then applied to a directional policy framework such as the GE/McKinsey Matrix (Figure 2.6)

What Figure 2.6 represents is the interconnectivity of the information and analysis models with decision-making frameworks, as modelled for use in a fuzzy logic or artificial intelligence environment. Whilst the actual creation of an artificial intelligence business decision-making model is still under development, the diagram indicates that it is both possible, and vital, to connect the output of analysis models (e.g. Porter's Five Forces) with the inputs of decision-making models (Directional Policy Matrix) which can then be used to select the appropriate framework (e.g. Ansoff's Growth Matrix) for developing the organisational strategy. The strength of each model comes from what it can contribute to the overall strategic decision-making system, rather than what it can do in isolation from the rest of the frameworks.

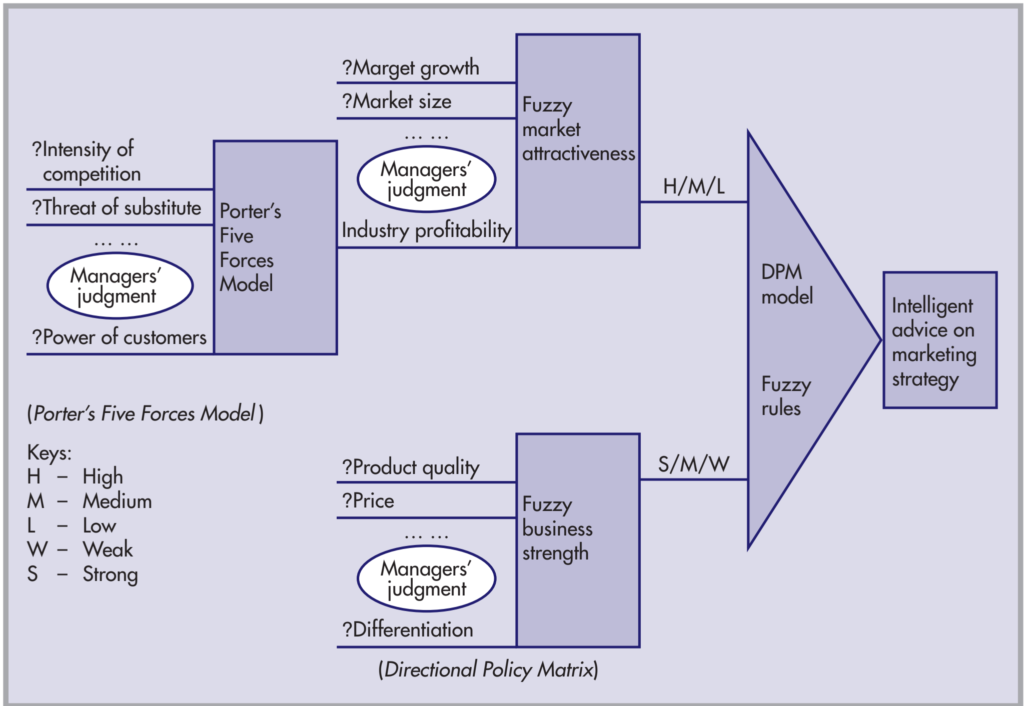


FIGURE 2.6 **Interconnected models**

Source: Reprinted from Li, S 2000, 'The development of a hybrid intelligent system for developing marketing strategy', *Decision Support Systems and Electronic Commerce*, 27, pp. 395–409, with permission from Elsevier.

Types of models

Marking models have a few recurring styles which are briefly overviewed here. These are:

- *structural equation models (SEM)*, which are predictive models based around sequences of dependent, interdependent and independent variables. The SEM is usually the result of a research using the LISREL or AMOS modelling software to demonstrate multiple influences on a single behavioural variable. Quite often, the SEM is used to test a hypothesis or two regarding the influence of one factor (e.g. speed of service) on a broader system of behaviour (propensity to buy beer at football games). These forms of models are expected to have an accuracy rate around 30 to 35% to be considered a good predictor of behaviour. Realistic expectations for SEM models focus predictive rates around 20%, so that a good SEM will be wrong four times out of five, and a great model will be inaccurate two thirds of the time. Consequently, while superior to random choice and luck, an SEM model is no guarantee of an outcome.
- *two-by-two matrix models*, which are the staple of marketing strategy, and include famous models such as the BCG Matrix. There are variants on the 2 × 2 framework, such as the 3 × 3 layout of the GE Matrix's strategic business planning grid. The matrix models usually measure broad factors such as 'time', 'market

share', 'profitability' along each axis, and divide the boxes into 'high', 'low' or similar semantically differential statements. Consequently, these models are less focused on predictive accuracy than they are on strategic guidelines. For example, a matrix examining cost and profitability would advise the termination of a product with 'low profitability' and 'high cost'. Whether this would lead to organisational success would not be covered by the model. That sort of question is usually addressed by SEM style analyses.

- *descriptive or illustrative models*, which are used to illustrate real world processes in oversimplified steps, such as the Belk (1975) behavioural intention model. These models have arisen either as pedagogical teaching tools or as conceptual models to use to examine how a process may work, but they are not designed to be predictive measures. Certain sections of the marketing and management academic body take great interest in attempting to measure the validity of these models. However, as the models represent abstract notions of the nature of the world, these are often quite difficult to translate into workable structural equation models.
- *bell curves, progressions or other mathematical line graphs with the word 'time' on one axis*. This includes Roger's (1995) innovator bell curve, the product life cycle model, and any number of models describing the movement of innovations through a community. In general, these types of models either describe cumulative effects (curves that sweep upwards) or population distributions (bell curves). To be polite, these are abstract mathematical creations designed to be illustrative indications of the flow of events in either a perfect world or a world constrained by numerous stated assumptions. These types of models can occasionally arise from observed data, although these are comparatively rare.

Metaphors and analogies: the value of models

Given that a good business model is like a set play in chess or a rehearsed movement in sport, certain preconditions must exist in the playing field for either to work. If those conditions are not met, then the set move will usually result in failure. Similarly, where the preconditions do exist, they are no guarantee of success. However, the purpose of a set play in sport is to provide a structured framework to use when engaging the opponent. Similarly, the purpose and value of a marketing model comes from its capacity to provide a structure to use as a basis for decisions. Business is a dynamic and shifting playing field at the best of times, and although market intelligence and market research has improved, most decisions are based on inaccurate, incomplete or insufficient data. Business decision making can feel like the equivalent of playing chess with half the board covered. Even though you can't see all of the pieces, you can maximise your opportunities with set moves and strategies based on the information at hand.

Limits of models

Many of the criticisms of marketing models come from the expectation that a mathematical or diagrammatic representation of the real world will accurately predict future behaviours.

The problem for any model of reality is the gap between the simplicity of a notion and the practicality of being able to implement that notion in real life. While the formulaic elements of business can be stated quite simply, such as 'Profit is the positive difference between revenue from sales and the cost of acquiring the sale', actually making a profit is certainly more difficult than it seems according to the definition.

Useful techniques for using marketing models

Strategic models are guidelines rather than hard and fast rules. Consequently, there are optimal methods for making use of the models for business planning and marketing strategy. A few of these methods are:

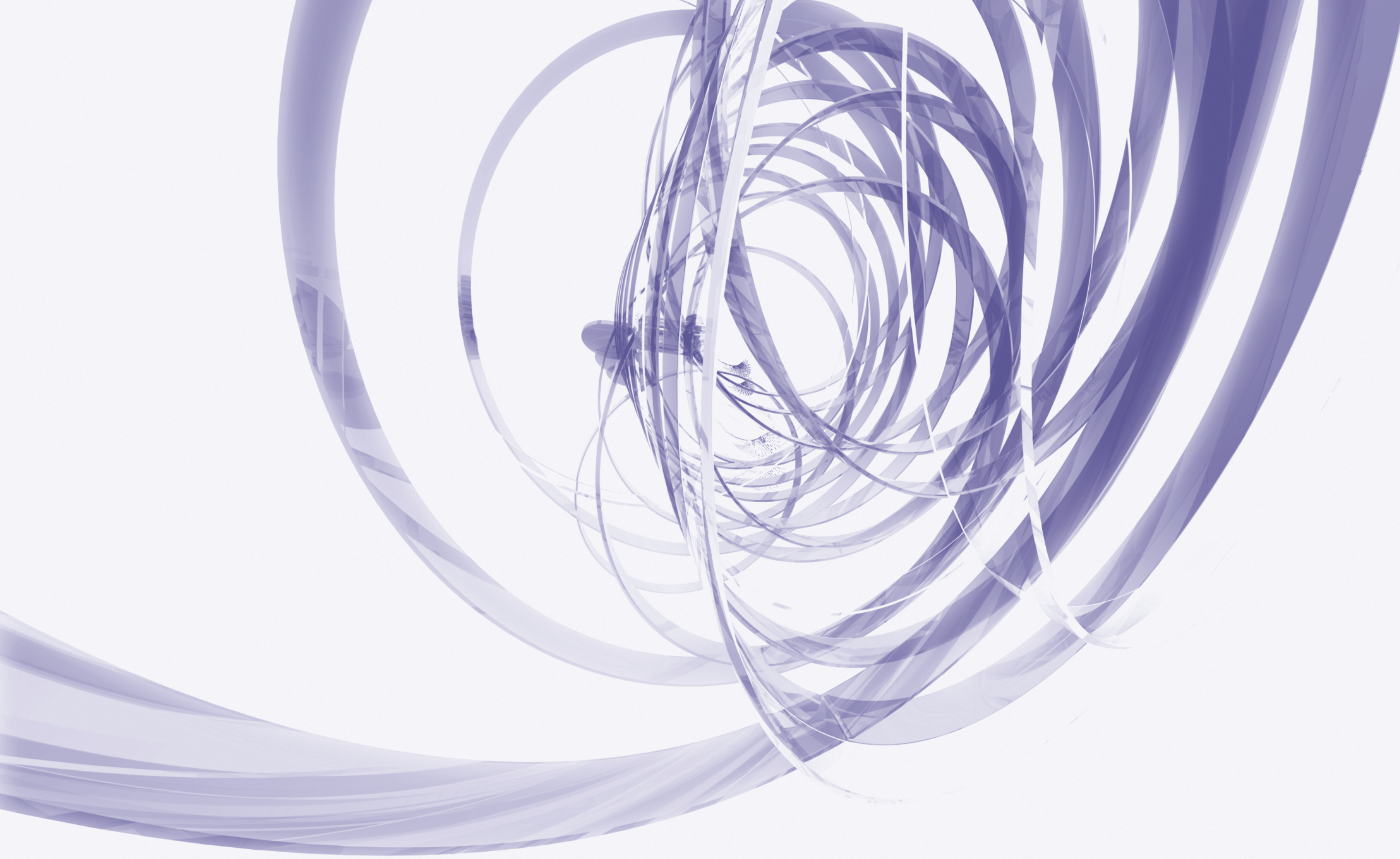
- Use multiple models when developing strategies. For example, simply relying on the product life cycle will only indicate where a product may currently stand. Using the PLC to assess where the product is and using the GE Matrix to determine the type of market and strength of the organisation allows the strategy to be set to make best use of market desirability, corporate capacity, and which type of curve (e.g. scalloped) is desired.
- Ensure the concepts are consistent across the models—one of the criticisms of the PLC is the lack of standards to determine what constitutes 'product' in the product life cycle. If the first model is analysed at the brand level, subsequent models need to be focused at the brand level.
- Look for divergence between the models, and explore that divergence. If one model suggests divesting, and another suggests growth, examine the steps by which the divergence came about. At a brand level, a product may be in decline as the brand is slipping in the market, however, the aggregate decline may not be matched by the rapid growth in one product, and the steeper declines in the other products.
- Assess the models at the product, brand, company, market and market demand levels as a starting point.
- Remember that the models are more like guidelines than codes of conduct. They are starting points to use when framing ideas for your organisation's specific needs, specific strengths and specific strategies, rather than scripts to be followed for perfect success.

Conclusion

Before developing a marketing strategy, you need to have a good understanding not only of core marketing concepts, but also of concepts and models in strategy. This chapter revises some common strategy models that are typically covered in introductory marketing courses, including Porter's Five Forces, Porter's Generic Competitive Strategies, the BCG Growth Share Matrix, the GE Matrix, Ansoff's Growth Matrix and the product life

cycle. Each model, its benefits and flaws, were critically analysed in light of their potential contribution to the development of marketing strategy.

Models are valuable conceptual tools that can help make sense of complex situations and provide options for strategic solutions based on years of research and observation. However it is critical to remember that the models are literally that—models. They represent an idealised version of reality and cannot be used as a formula for policy development. For example, while research into marketing practice shows that developing a new market will require relatively high levels of expenditure on marketing communications, increasing the advertising budget does not guarantee success. Ultimately the models provide useful guidelines to help structure options for strategy development.



PART 2

Doing the groundwork

Marketing and stakeholder selection

CHAPTER 3

Introduction

The explicit inclusion of stakeholder benefit in the 2004 definition of marketing means that stakeholder selection is now an integral part of the strategic marketing process. Consequently, it is a strategic priority to be able to identify the organisation's stakeholders, and to be able to rank their relative importance to the core business and mission of the organisation. While every stakeholder has a potential impact on the organisation, in any given situation only a few stakeholders will have the relevant urgency, power or legitimacy to have a genuine impact on marketing strategy development. This chapter covers a model of stakeholder selection, stakeholder analysis and revisits the characteristics of the stakeholder. In addition, a selection of stakeholder types will be examined, and although this is not a complete list, it gives an indication of the breadth and depth of the exercise involved in stakeholder selection.

The nature of stakeholders

As mentioned in Chapter 1, stakeholders are an integral part of the marketing definition and, as a result, some of the material presented in this section will be familiar from the first chapter. One of the common judgement errors exhibited in marketing strategy and marketing

education is to treat familiar information as less important than new concepts. Given the increased involvement of stakeholders in marketing and marketing strategy, the relative importance of each stakeholder group will be emphasised throughout the text, since it will be both valuable in business, and highly likely to be an examinable question in assessments.

Stakeholder context

There are different stakeholder groups defined in this chapter. These groups range from the macro level influences of society and government, through to the micro level stakeholders such as employees, managers and customers. Consequently, deciding which stakeholder is most significant in a given situation will require both effort and a consistent framework to apply across all stakeholder types. Stakeholders can be clustered into broad categories based on the context in which they interact with the organisation.

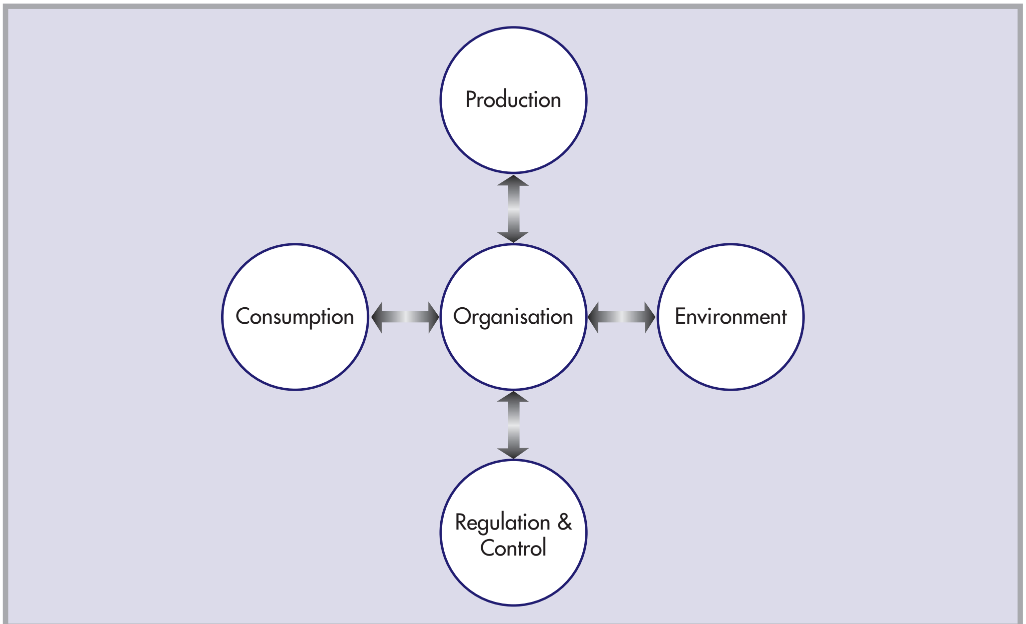


FIGURE 3.1 Stakeholder contexts

There are four contexts for interaction between the firm and the stakeholder (Figure 3.1):

- *production context*, which includes everyone involved in sourcing the component parts for making the product (e.g. suppliers), being part of the organisation (investors, boards of directors, shareholders, employees), or providing the distribution networks (distributors)
- *consumption context*, the actual purchase and use of the product, and largely consists of the consumers, although it may include wholesalers and resellers
- *environment context*, which includes social norms, acceptable standards and the broader community including competitors in the marketplace, social pressure groups and the media

- *regulation and control context*, which covers self-regulation, membership of associations and marketing boards, and the role of governments in setting legal parameters for the marketplace.

Establishing the stakeholder context is a vital part of determining which stakeholders are most important in a given situation, and what benefit each can be expected to receive from the marketing activity of the organisation. For example, setting the strategic objectives of a business will involve the production context, whereas determining a strategic response to new advertising regulations will focus on the regulation and control context.

Ranking criteria for stakeholders: power, legitimacy and urgency

Mitchell, Agle and Wood (1997) propose a three-part model to determine the relative importance of stakeholders. Figure 3.2 outlines their model, mentioned in Chapter 1, in which each stakeholder is assessed according to the following criteria:

- *power*, or to the extent to which the stakeholder can assert their will over the organisation (Maignan, Ferrell & Ferrell 2005)
- *legitimacy*, or the appropriateness of the stakeholder's actions towards the firm
- *urgency*; the degree to which the actions of the stakeholders require an immediate response, or where the response is time sensitive in nature.

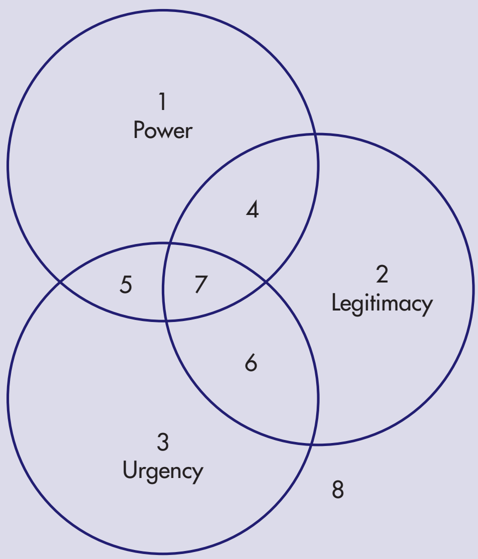


FIGURE 3.2 **Classes of stakeholders (1)**

Source: Mitchell, RK, Agle, BR & Wood, DJ 1997, 'Toward a theory of stakeholder identification and salience: Defining the principle of who and what really counts', *The Academy of Management Review*, Oct. 22, (4) pp. 853–86. Reproduced with permission of Academy of Management (NY).

Power in this context is referred to as the ability of the stakeholder to exert their will over the organisation, and arises from a combination of three source groups (Yukl 1998):

- *position power*, derived from a combination of formal authority, control of rewards, or control over the administration of punishments
- *personal power*, the power derived from human relationships and the interaction of people, including factors such as charisma, friendship, loyalty or expertise
- *political power*, the power arising from the convergence of opportunity and the objectives of the two parties (e.g. mutual benefit), or control mechanisms such as control over decision-making processes, coalitions of shared interest, and/or co-option, or formally vested power.

These three forms of power can be combined to create seven different types of power, as outlined in Table 3.1.

TABLE 3.1 Types of Power

Type of power	Composition	Definition
Coercive	Position power	Compliance is enforced through punishment
Connection	Personal + political power	Based on interpersonal links or links to important people
Reward	Position power	Compliance is encouraged through rewards
Legitimate	Position + political power	Organisational or hierarchical power structures
Referent	Personal power	Personal traits such as charisma or interpersonal influence
Information	Position + personal + political power	Possession or access to valuable information
Expert	Personal power	Expertise, skills, knowledge which are used to gain respect

Source: Adapted from Greene & Elfrers 1999, *Power the 48 Laws*, London, Profile Books.

From a marketing perspective, a stakeholder may exhibit each of these forms of power over the business. The value for marketing is to determine the method and type of power being exerted by the stakeholder to examine the extent to which this also determines the urgency and legitimacy of the activity. For example, coercive power is likely to be used where the stakeholder lacks legitimacy, but is seeking urgency. In contrast, information and expert power may also indicate legitimacy, although it may not hold as much urgency as a coercive power display. The interaction of the three stakeholder attributes is explored below.

Stakeholder typology based on stakeholder attributes

Setting the relative importance of a stakeholder is a three-part process. First, the organisation needs to consider the context in which it is dealing with the stakeholder. Is the stakeholder the customer, or are they a part of the organisation, part of the marketplace or an external regulatory influence? Second, the organisation needs to determine the relative importance of one stakeholder over another on the criteria of legitimacy, power and urgency. Finally, the organisation needs to allocate a relative priority order of stakeholders based on the context and the influence each stakeholder has over the organisation. This initial analysis then leads to the assignment of each stakeholder into one of the following categories (illustrated by Figure 3.3).

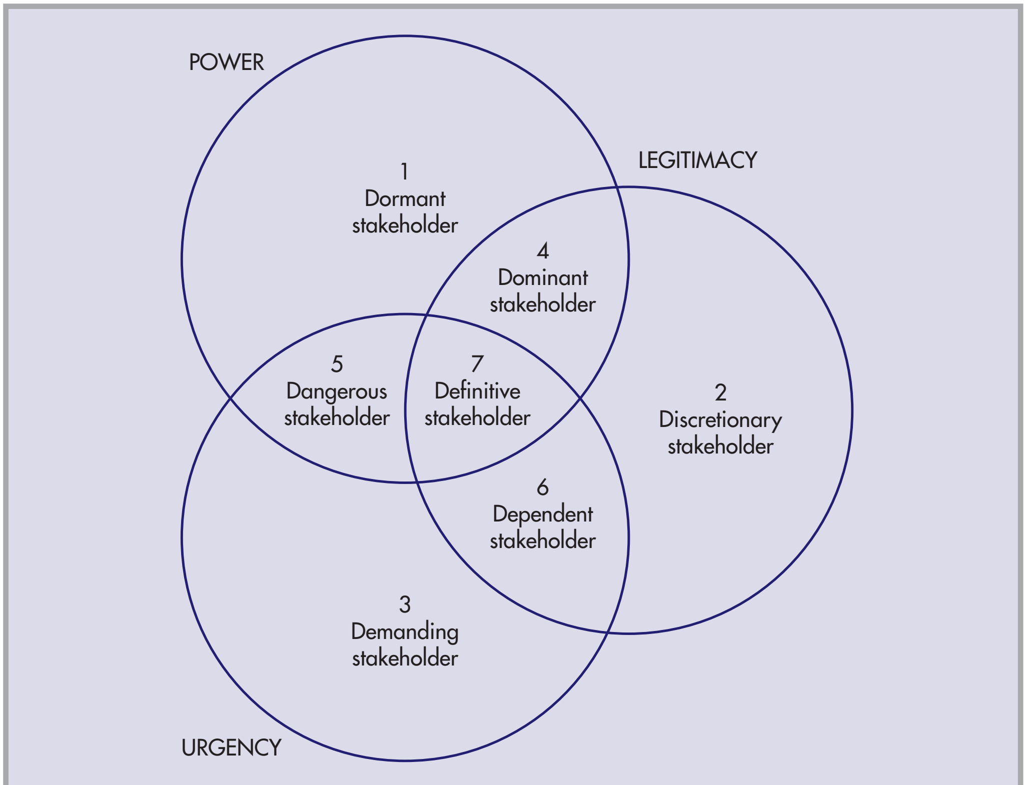


FIGURE 3.3 **Classes of stakeholders (2)**

Source: Mitchell, RK, Agle, BR & Wood, DJ 1997, 'Toward a theory of stakeholder identification and salience: Defining the principle of who and what really counts', *The Academy of Management Review;* Oct. 22, (4) 853–86. Reproduced with permission of Academy of Management (NY).

The 7 stakeholder groups are:

- *Dormant stakeholders*: those stakeholders who would have power over the organisation, but who do not have a legitimate relationship nor an urgent claim, and as a result, their power is unused. For example, a disgruntled former employee

with access to corporate secrets has power over the firm should they elect to use this knowledge, however, on acting on the knowledge they would become either a dangerous stakeholder (non-legitimate use of the power) or a dominant stakeholder (legitimate use of the power).

- *Discretionary stakeholders*: those stakeholders who have a legitimate claim, yet lack the power or urgency to influence the organisation. Although there are no pressing needs (urgency) or threats (power) to force an interaction, these stakeholders can be addressed by the organisation, for example, via corporate philanthropy or similar corporate citizenship activities.
- *Demanding stakeholders*: who present a level of urgency, but lack either the power to exert their will, or the legitimacy to be addressed. Quite often, this can include protest actions or negative websites that make claims that cannot be contested legitimately or which do not have any power behind their threats.
- *Dominant stakeholders*: those groups that have an influence over the firm through power and legitimacy, but who are not active in pursuing this influence. These stakeholder groups can include investors, boards of directors, governments and suppliers/distributors. The needs of these stakeholders are often addressed as implicit goals of the organisation, insofar as their needs do not conflict with the needs of the definitive stakeholder.
- *Dangerous stakeholders*: stakeholders who possess power and urgency, but lack any form of legitimacy to their claim. Understandably, the dangerous stakeholder can harm the firm, for example, an extortion threat has power and urgency without legitimacy. Effectively, any form of coercion or threatening behaviour by a stakeholder which is marked by urgency (current active threat) and power (capacity to act on the threat) positions that stakeholder as a dangerous influence to be addressed, defused or defeated.
- *Dependent stakeholders*: stakeholders who have legitimate and urgent needs, but no power to influence the organisation. This group often requires the guardianship of the stakeholders who exercise legitimate power over the organisation, e.g. vulnerable consumers who have legitimacy and urgent needs often have these needs enforced by the government, which supplies the necessary power to assist the group.
- *Definitive stakeholders* are the type of shareholder who has all three aspects—a legitimate claim, which is urgent, and which can be enforced due to the stakeholder's level of power over the organisation. Definitive stakeholders can be hybrid or compound stakeholders, e.g. a dependent stakeholder supported by dominant or dormant stakeholder.

Addressing the stakeholder situation can be complicated For example, a vocal parental lobby group wanting restrictions on fast food advertising to children may be perceived as having legitimacy and urgency (dependent stakeholder). Alternatively, the group could be perceived as simply a nuisance with neither legitimacy nor power (demanding), or threats of boycotts made by the group could be seen as power (dangerous). Finally, if the

organisation deemed the needs of the group to be legitimate, the group could be either discretionary stakeholders (neither power nor urgency), dependent (legitimacy, urgency and no power) or definitive stakeholders. Understandably, classification of stakeholders into their respective categories is situational, and requires the organisation to carefully consider the relative priority and composition of the priorities of the stakeholder.

Understanding the relative levels of power, legitimacy and urgency

Neville, Menguc and Bell (2003) adapted and upgraded Mitchell, Agle and Wood's (1997) original three rating construct (Figure 3.4).

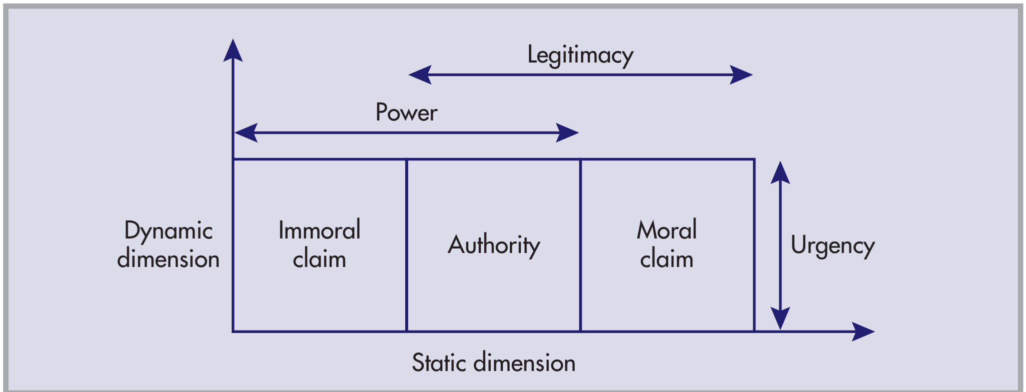


FIGURE 3.4 **Stakeholder claims (power and legitimacy)**

Source: Neville, BA, Menguc, B & Bell, SJ 2003, *Stakeholder salience reloaded: Operationalising corporate social responsibility*, Australia New Zealand Marketing Academy Conference, Adelaide, December 1–3.

Neville, Menguc & Bell (2003) created three levels of claim based on power and legitimacy, each of which was influenced directly by urgency. Urgency in the context of Neville et al.'s (2003) framework was the immediacy with which the firm had to act, and it was seen as a multiplier effect on the influence of the stakeholder's claim. For example, a moral claim with a high urgency was more likely to be addressed than a claim by an authority that was less urgent.

The urgency of a claim had also been supported elsewhere as the best predictor of response (Agle, Mitchell & Sonnenfeld 1999). Clement (2005) further enhanced the value of urgency as a predictor by including the relative power of the stakeholder in the situation. However, before urgency became the sole determinant of the response, Frooman (1999) suggested that the relative power of the stakeholder varied by the level to which the organisation was dependent on the stakeholder, and that dependency influenced urgency and power. Consequently, membership of the 'production function' stakeholder context such as shareholders, employees and customers could wield additional power based on the organisation's dependency on them, as well as their power, legitimacy and urgency. In conjunction, this creates a complex model of the stakeholder influence, which is illustrated by Figure 3.5.

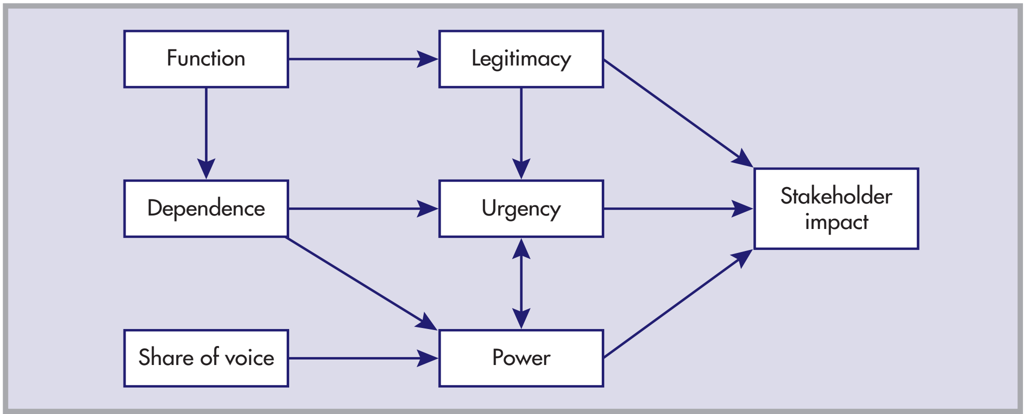


FIGURE 3.5 A model of predicting stakeholder impact

The components of the model are as follows:

- *stakeholder impact*, which is a rating of how much influence the stakeholder has on the organisation in this situation. Given the nature of stakeholder influence, this impact changes between different situations—for example, the launch of a new product into a new market will have a different set of stakeholder influences when compared to the withdrawal of a low-selling product from an existing market. This is the output of the model, and would tie back into the stakeholder typology (Figure 3.3 above).
- *legitimacy*; the appropriateness of the stakeholder's actions towards the firm, whether these actions are desirable, within socially accepted norms, or consistent with wider society expectations.
- *function*, or the role the stakeholder plays in the organisation. Function is subdivided into product, consumption and environment. Production includes those elements that are direct influences on the creation of the product, such as suppliers, employees, and managers. Consumption refers to those stakeholders who actually use the organisation's product. In business to business, this may be split into the purchasing stakeholder (e.g. organisational buyer) and the end user (clients). Environment represents the stakeholders who do not directly influence the production or consumption of the product, but who assist in the creation of the society and social norms in which the product is sold, e.g. local communities, lobby groups and governments.
- *urgency* is the degree to which the actions of the stakeholders require an immediate response or can be delayed, and where the response has a time sensitive nature. This can be directly influenced by the organisation's dependence on the stakeholder insofar as stakeholders on which the company depends will receive greater priority.
- *dependence* is the extent to which the organisation relies on the stakeholder for a core aspect of its functionality or survival. This element influences the level of

urgency with which the stakeholder's needs should be met, and the amount of power that resides with the stakeholder. For example, a manufacturer with a heavy dependence on its suppliers for specialist parts will need to respond quickly to the supplier's needs, and will concede considerable power to the supplier. Dependence is also influenced by function. For example, the stakeholder influence of employees who cannot be easily replaced will be greater than the influence of an external lobby group. Stakeholders from the consumption function (e.g. consumers) or production function (e.g. employees) are more likely to exert a stronger influence than those from the indirect areas such as the environment (e.g. lobby group).

- *power*, which refers to the extent to which the stakeholder can assert their will over the organisation. Power interconnects with urgency, as the level of influence can be used to force the organisation to change priorities to meet the need of the most powerful. Power is influenced by the dependence between the two parties (e.g. the greater the dependence of the organisation on the stakeholder, the more power the stakeholder holds), share of voice (the ability of the shareholder to influence public opinion through the ability to speak freely).
- *share of voice*, or the ability of the stakeholder to speak freely to the organisation or other stakeholders through the media, internet or other means of communication. Share of voice indicates the extent to which the stakeholder can control the agenda in public debate, or can get their message across, and consequently impacts on the power that the stakeholder can wield over the organisation. Share of voice consists of the two major influences of mobilisation and representation. Mobilisation is the ability of the stakeholders to organise themselves and present a united front or unified message to the media and broader community. Representation is the size of the shareholder group being represented, for example, a citizen action group representing local residents, or an industrial workers union representing employees across the country.

Making use of the model

The purpose of this model is to assist in setting a relative level of importance for each stakeholder in a given situation. For example, when assessing the influence of stakeholders on a marketing strategy, the model works through a series of questions, such as:

- What power does the stakeholder have over the organisation?
- How urgent are the requests?
- How legitimate is the stakeholder's influence?

Power over the organisation

In this model, power is based on the ability of the stakeholder to assert their will over the organisation. As one of the three key rating criteria, power is assessed in its own right, and on the basis of the additional influences from share of voice and dependence. In addition, urgency can increase the power of a stakeholder's influence, particularly where a crisis event occurs, and stakeholders need to be addressed.

Judging the influence of a stakeholder over the firm can be assisted by assessing the level of the firm's dependence on the stakeholder, and their share of voice.

Dependence is also influenced by the function of the stakeholder, for example, an organisation is more likely to be dependent on a stakeholder who is involved directly in the consumption process than on a stakeholder who forms part of the broader social environment, although this can vary by circumstance. Similarly, involvement in the production function increases the likelihood of the organisation's dependence on the stakeholder, when compared to the broader community.

In contrast, share of voice represents the profile of the stakeholder, and their ability to speak unhindered by the actions of the organisation. Prior to the widespread adoption of the internet, the share of voice was relatively easily assessed in terms of access to radio, print media and television. Now, additional influences such as websites, blogs and email campaigns have expanded the ability of any concerned group to speak out, and command a share of voice. Share of voice is also a factor of the size and power of an organisation in terms of whom they represent, and their capacity to mobilise their membership. Of the two factors, mobilisation is likely to have the greatest influence on the share of voice, as a well-organised small stakeholder group using their share of voice can exert a high level of power and influence over an organisation.

Urgency of the request

Urgency is the speed with which an organisation should respond to a stakeholder's influence. This response is influenced by the legitimacy of a stakeholder and their level of power. Agle, Mitchell and Sonnenfeld's (1999) survey of 80 CEOs found that real-world pragmatism and pressure led to the urgency of a stakeholder's impact being the best predictor of their level of influence. Urgency is heavily influenced by the level of dependency an organisation has on the stakeholder. The greater the dependence the organisation has, the more likely they are to perceive the stakeholder's impact as urgent, and respond to that stakeholder's issues ahead of other stakeholders who were perceived as less powerful or influential. In this context, Agle, Mitchell and Sonnenfeld (1999) concluded that the function of the stakeholder has the greatest impact on the level of dependence, which in turn influenced the urgency.

Legitimacy of the stakeholder

In a perfect world, legitimacy would be the top priority of an organisation when assessing the impact of a stakeholder. In reality, legitimacy is often the lowest priority, having little more impact than influencing the perceived urgency of a stakeholder's issues. Legitimacy consists of the appropriateness of the influence, the broader social support for the position held by the stakeholder, and the function of the stakeholder in the organisation. Core functions, such as consumption or production, are assumed to have greater legitimacy ahead of the external stakeholder influences of the environment context. That said, the relative ineffectiveness of legitimacy is evidenced when non-representative organisations with strong share of voice and effective power, and low legitimacy have a larger impact on the organisation. For example, in Australia, the anti-speeding lobby groups have caused

television advertising for high-speed vehicles to be modified or withdrawn despite their position not being based on a high level of legitimacy (a small group promoting a non-representative opinion). Whilst the broader community and the internal influences of the car manufacturer and car advertiser regard the advertising as acceptable, the legitimacy of their influence is outweighed by the power of the anti-speeding lobby.

Key stakeholders

This section of the chapter addresses a variety of pre-existing types of stakeholder groups. Whilst the relative power, urgency and legitimacy of stakeholder varies according to the context of the business and situation, some consistency exists in the types of stakeholder groups that can be encountered. These stakeholder groups are listed in broad categories that define a functional role for the stakeholder, for example, as creditors or customers. In a stakeholder analysis, creditors would be listed specifically, e.g. Esanda or Suncorp-Metway. Similarly, whilst generic descriptions of the expectations of stakeholders are provided here, they are a starting point to consider the needs and wants of the organisation's stakeholders.

Stakeholder maps

Stakeholder maps are one method of determining the influence of key groups on the organisation, and the key issues that will be of importance to that group. Scholem and Stewart (2002) outlined a stakeholder mapping process where the generic stakeholder groups were initially clustered onto a generic map (Figure 3.6), with emphasis given in the original paper that each stakeholder can be further subcategorised (e.g. media can be local, national or specialist media) to improve the depth of the map.

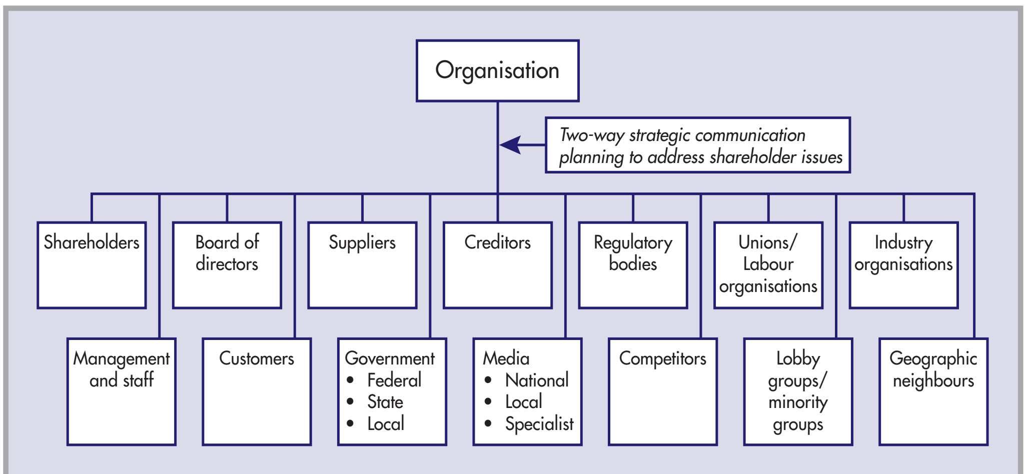


FIGURE 3.6 **Stakeholder map**

Source: Scholem, P & Stewart, D 2002, *Towards a Measurement Framework for Stakeholder-Issue Identification and Salience*, Australia New Zealand Marketing Academy Conference, Melbourne, December 2–4.

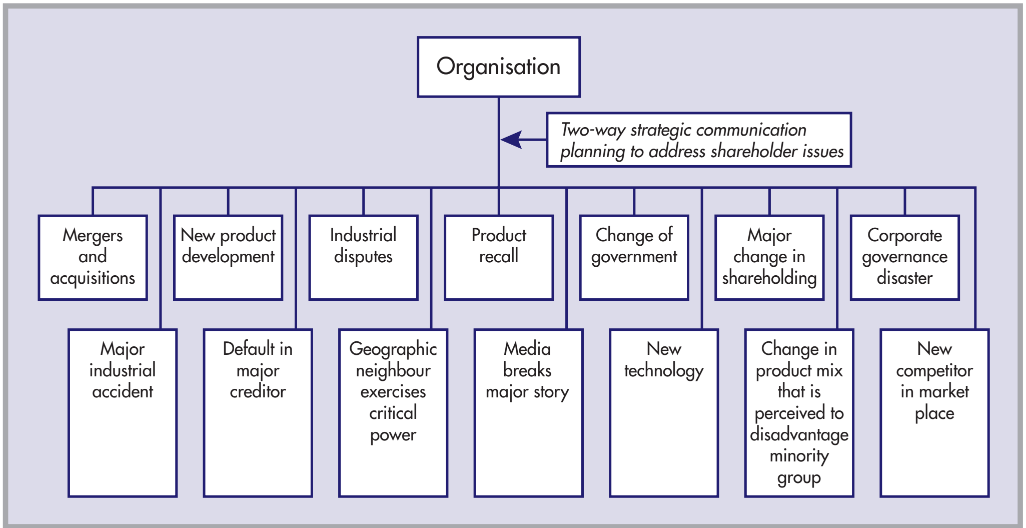


FIGURE 3.7 **Stakeholder issues map**

Source: Scholem, P & Stewart, D 2002, *Towards a Measurement Framework for Stakeholder-Issue Identification and Salience*, Australia New Zealand Marketing Academy Conference, Melbourne, December 2–4.

Using the initial map as a base, a second map of the key issues is developed, in which each stakeholder cluster is assessed based on issues, problems or opportunities that each group presents to the organisation. An indicative issues map is illustrated in Figure 3.7.

The issues map can be used to assist strategic planning in that the organisation can use it to highlight where possible conflicts may arise between the current or proposed strategy, and the marketing objective of providing benefit for the organisation and its stakeholders. Further, the map can be used to assist in the prioritisation of stakeholder issues based on how the identified stakeholder issues are rated on the power–urgency–legitimacy framework outlined above. Completing the stakeholder issues map requires an understanding of how the different stakeholder groups interact with the organisation.

Active, passive and switch stakeholders

Fifteen different types of stakeholders have been identified from the broader marketing and management literature. These are examined in terms of the primary context in which they would be expected to be engaged (e.g. production or consumption context), and whether the stakeholder is active, passive or capable of switching between these positions. Stakeholder type, primary context and their status type is summarised in Table 3.2.

The primary context is the usual environment in which the organisation would be expecting to deal with the stakeholder and their issues. This is not to say that a stakeholder cannot be a member of more than one context, for example government can be in the consumption, environment and regulation and control contexts. However, the dominant area that would be expected is for the government to be a stakeholder in the regulation and control context.

TABLE 3.2 Stakeholders, context and the passive/active dichotomy

Stakeholder	Primary context	Status type
Board of directors	Production	Active
Competitors	Environment	Switch
Creditors and financiers	Production	Active
Customers	Consumption	Switch
Distributors	Production	Switch
Employees	Production	Active
Government	Regulation and control	Passive
Local community	Environment	Passive
Managers	Production	Active
Media	Environment	Passive
Shareholders	Production	Active
Social pressure lobby groups	Environment	Passive
Society/citizens/community	Environment	Passive
Suppliers	Production	Switch
Unions	Production	Switch

The three categories of activity are based on a dichotomy outlined by Grimble and Wellard (1997). Passive stakeholders are influenced by the organisation's actions whereas active stakeholders exert an influence over the organisation's activities. In addition to the Grimble and Wellard (1997) dichotomy, the third category of 'switch' stakeholders is included. Switch stakeholders are those who can shift between passive and active depending on the situation and context. For example, customers are usually passive where the firm is making minor upgrades to a product due to technology upgrades, and are usually active when their market needs are being directly addressed in co-production. Switch stakeholders are determined on the basis of the context within which they interact with the organisation.

The following section examines the different stakeholder groups, including the generic expectations that these groups would normally have in regards to the organisation. As a general rule, these descriptions are reasonably broad, generic, and need to be adapted to the specific details of the organisation's actual stakeholder groups. As with the strategy models of Chapter 2, these categorisations are starting points for the marketing manager, rather than definitive solutions to the question of 'who are the organisation's stakeholders?' The list of stakeholders examined includes:

- board of directors
- competitors
- creditors and financiers
- customers
- distributors

- employees
- government
- local community
- managers
- media
- shareholders
- social pressure lobby groups
- society/citizens/community groups
- suppliers
- unions.

Board of directors

Boards of directors are usually expected to play an overview role in an organisation. As such, they are theoretically expected to review the strategic direction of the organisation, whereas Kaplan and Norton (1996) indicate the reality is that the board is far more likely to be focused on the financial statements of the organisation than the overall strategic direction. As part of the production context, the board of directors is able to directly influence the strategic goals of the organisation, through querying financial performance, the allocation of resources or reviewing the strategic plans.

- *Expectations*: profit versus strategic goals, shareholder value, organisational longevity
- *Context*: production
- *Active/passive*: active

Competitors

Competitors are any other providers of similar value solutions that the consumer can use instead of the organisation. The 2004 definition of marketing has changed the notion of the competitor from any rival product provider, to any rival value solution for the customer. As a result, where organisations previously saw competitors in terms of products or services, they now have to assess competitors as rival methods by which the consumer can meet their needs and wants by receiving 'value'. Competitors are considered passive participants in the environmental context as they cannot directly influence strategic decisions although they may influence short-term tactics. Whilst a competitor can react to the organisation, it remains a passive participant under Grimble and Wellard's (1997) definition of passive as being where a stakeholder is influenced by the organisation's actions.

- *Expectations*: competition, market development, product development, self-regulation and industry based lobbying
- *Context*: environment
- *Active/passive*: switch

Creditors and financiers

These two groups represent those stakeholders who have a financial interest in the organisation through loans, unpaid debts or other legal claims over the organisation's assets. Creditors can directly influence the activities of the organisation through requests for repayments, provision of lines of credit to purchase products, or allowing the deferral of repayments where the organisation is in financial difficulty. The major influence of the creditor and financier group remains in the production context as these two groups provide the financial resources to allow the organisation to operate. As a point of differentiation, financiers have actively sought to be involved in the organisation by providing funds whereas creditors can arise from one organisation owing money to another organisation.

- ***Expectations*: fair disclosure, return on investment, profit versus non-economic goals, accounting policies, repayments**
- ***Context*: production**
- ***Active/passive*: active**

Customers

Customers are a complex stakeholder group. In one sense, they are an active participant as the organisation seeks to offer something of value to them, to satisfy their needs and wants, so the organisation can benefit from an ongoing relationship with the customer. At the same time, customers are also passive participants insofar as they do not always exert direct influence over the actions of the company. For example, whilst the consumer is the end recipient of an innovative product, the innovation itself may have been created by the organisation, rather than derived from the actions of the customers. Further, in business to business relationships, customers can also be involved in co-production of products and ongoing marketing relationships where they directly influence the firm's activities. Finally, to confuse the issue further, in business to consumer transactions and relationships, an individual may be a customer, employee, local community member, shareholder and member of a social lobby group trying to influence the organisation. However, despite the complexity of the consumer, there are a few consistent factors that the consumer seeks, which include the ongoing satisfaction of their needs and wants and the value exchange of paying for a product that meets those needs or wants.

- ***Expectations*: ongoing satisfaction of needs and wants, safety, fair disclosure, quality, delivering the promised value proposition, meeting post-sale obligations**
- ***Context*: consumption**
- ***Active/passive*: switch**

Distributors

Distributors are participants in the production context who hold both passive and active roles as stakeholders. In recent years, the concentration of ownership of distribution channels has led to a rise in the active role of the distributor, as their willingness or unwillingness to carry a product will have a significant impact on the organisation's ability to do business. In the United States, Walmart was able to use its size and purchasing power to dictate changes to the cover art for various music CDs along with altered track content (e.g. the censored radio edit editions rather than traditionally uncensored album versions of the songs). However, the average distributor is not as powerful, or as likely to directly influence the production context in the way Walmart has, and consequently, can also be passive participants in the process.

- ***Expectations*: freedom from undue influence, good faith in negotiations, meeting demand, supplying product to deadlines**
- ***Context*: production**
- ***Active/passive*: switch**

Employees

Employees are a separate stakeholder group from management, directors and shareholders as they have a differing set of priorities to the other internal organisational stakeholders. Unlike shareholders, employees are heavily dependant on the organisation for financial gain, and are subject to the power of the management and directors. However, as the people ultimately responsible for the creation and delivery of value to the customer, they play a vital role in the survival of the organisation. Consequently, whilst they can be passive in certain circumstances, it is their direct influence on the creation of the product that usually makes them an active participant in the production context.

Employees are also similar to customers as stakeholders who are members of multiple stakeholder groups. For example, an employee can be a shareholder, union member, customer, lobby group member and member of the community. As the stakeholder group that the organisation wields the most direct influence over, they are also one of the largest assets in managing multiple stakeholder demands, particularly between the organisation and the customer stakeholders.

- ***Expectations*: ongoing employment, wages, workplace health and safety standards, privacy, codes of conduct, employment conditions, protection from unfair treatment and unfair dismissal**
- ***Context*: production**
- ***Active/passive*: active**

Government

Government exists at multiple levels in Australia and New Zealand, and whilst the dominant power comes from the federal level, the impact of state and local governments makes them significant stakeholders in the organisation. Although government is part of the regulation and control context, it can also act as a consumer for the organisation. For simplicity's sake, governments buying from the organisation are treated as consumer stakeholders. In a socialist nation, or an economy with nationalised industries, governments would be active stakeholders. Where a government owns an enterprise such as Queensland Rail or the Melbourne Ports Authority, the corporatisation of these entities means that the government is effectively a shareholder, or part of the board of directors, and is dealt with in the context of those stakeholder groups. Similarly, whilst regulation and law can force product changes or strategic direction, government is listed as passive as it tends not to take an active controlling influence in business under the current political regimes. Whilst the Australian and New Zealand governments do not tend to directly interfere with business strategies, both governments do set the broader economic agenda through financial policies.

- *Expectations*: compliance with the laws of the country, role of business in politics, economic activity in line with government policy
- *Context*: regulation and control
- *Active/passive*: passive

Local community

The local community stakeholder is an environmental influence over the organisation in that it represents a focused segment of the broader society in which the organisation operates. For most organisations, the local community is defined by the proximity it has with the head office, plants, factories or shops. Other determining factors include areas where one organisation dominates the local employment market, e.g. mining towns, or townships based around ports, army bases or other major employment sources. The role of the local community as a stakeholder is to represent the composite interests of the people affected by the organisation's decision, for example, the families of the employee stakeholders, or the local businesses that provide services and goods to the employee stakeholders (rather than being supplier stakeholders to the organisation). Local communities are also a subset of the broader stakeholder group of society/citizens/broader community.

- *Expectations*: community obligations, location of organisational buildings such as factories or offices, employment opportunities, contribution to local economy, community consultation
- *Context*: environment
- *Active/passive*: passive

Managers

Managers are a specific class of stakeholders who hold more influence and power in the organisation than the employee stakeholders, but who are also part of the overall organisational structure. Whilst managers are often responsible for implementing strategies that impact on other stakeholders, they may or may not be directly responsible for the creation of those strategies. For example, the board of directors, acting on the influence of the shareholder stakeholders, may set the direction of the organisation to downsize and reduce costs. The management stakeholders are then responsible for implementing the downsizing, so whilst they can have a direct impact on the employee stakeholder (selecting the employee for redundancy), they may have little control over the overall process (reduce the workforce by 15%). The management stakeholder group should be considered whether the strategy comes from outside of that stakeholder group (board of directors) or from the management, so that the impact is measured appropriately. Unlike most stakeholders, however, management tends to have the earliest opportunity to be involved in the process, and can often wield significant power in the relationship.

- ***Expectations*: job security, freedom to follow through organisational plans, consultation where an objective or activity will impact on an area of responsibility**
- ***Context*: production**
- ***Active/passive*: active**

Media

The media stakeholders are split into three groups:

- *'traditional media'*, which includes radio, television and newspapers
- *new media*, which consists of the internet, including online news sites and websites, and which can be clearly traced to an organisation, company or other corporate owner
- *independent self-publishing*, which includes blogging and other non-organisation based self-publishing.

The distinction between new media and independent self-publishing is the ownership of the media vehicle. Independent vehicles, such as blogs, online journals and personally owned websites are now able to compete for share of voice as media, due to the widespread adoption of the internet and the efficiency of web search engines. For example, searching Google for an organisation's brand name can bring up official corporate websites, independent commentary, and branded items for sale on eBay with equal ease. Consequently, the media stakeholder is a broader category than just the traditional investigative journalist or finance pages commentator.

- *Expectations*: honesty, business integrity with consumers, responsiveness, newsworthy stories
- *Context*: environment
- *Active/passive*: passive

Shareholders

Shareholder stakeholders have a financial interest in the organisation, and as such tend to have a relationship with the firm based on the return on investment that the firm can provide. Although some shareholders can base their portfolios on non-financial objectives such as ethical investing, or environmentally friendly investing, the investments within those narrowed parameters are still expected to be revenue raising, rather than charitable donations. Whilst the influence of the shareholder as a stakeholder is significant, and subject to measures such as the shareholder value analysis, the dominant interest for shareholders is financial return.

- *Expectations*: fair disclosure, profit versus social/environmental goals, moderation of directors' bonuses, costs, ethical investments, return on investment
- *Context*: production
- *Active/passive*: active

Social pressure groups/lobby groups/interest groups

The stakeholder category of social pressure groups, lobby groups and interest groups is a catch-all category for any organised group of people who are not part of the organisation or government, but who are attempting to influence the organisation's goals and objectives. For example, Greenpeace is a social pressure group that tries to influence the organisation's behaviour towards the environment. In general terms, any group with a specific agenda that attempts to influence the behaviour of the organisation to act on that agenda (e.g. reduce use of leaded petrol by the Lead Education and Abatement Design Group) can be considered part of this broad stakeholder group.

- *Expectations*: consideration of specific social interests such as gender equity, environmentalism, racial discrimination or other social pressure issues
- *Context*: environment
- *Active/passive*: passive

Society/citizens/broader community

The society/citizen/broader community group is the stakeholder catchment that represents the general views, beliefs, opinions and social structure of the wider society in which the organisation operates. Unlike the previous category, 'society' is not structured as a formal grouping or organisation. The major influence this category plays is in setting the broad social norms for the marketplace, such as the political structure (democracy, totalitarianism), broad social tolerances (e.g. gender roles), influence of religion, social taboos and similar broad areas. For the most part, this stakeholder group is only an influence where the organisational goals and objectives will knowingly contravene a social standard—for example, establishing a race- or gender-segregated service, or producing a harmful product aimed at minors.

- ***Expectations***: **corporate philanthropy, support for underprivileged/minority groups, ethical behaviour, contribution to the economy**
- ***Context***: **environment**
- ***Active/passive***: **passive**

Suppliers

Suppliers are an integral part of the production process as they deliver the materials that are used to create the organisation's value offering to the customer. Consequently, suppliers can exert a level of power and influence over the organisation, although at the same time, the organisation is the customer stakeholder for its suppliers. The resulting balance between supplier power and consumer power is a major part of the relationship marketing dynamic of reciprocity.

- ***Expectations***: **freedom from undue influence, good faith, tendering processes, business relationships**
- ***Context***: **production**
- ***Active/passive***: **switch**

Unions

Unions represent the collective interests of their workers, who are themselves individually part of the employee stakeholder group. The role of the union as a stakeholder includes representing the rights of the employees across a business sector, rather than just in the specific organisation. Unions tend to become major stakeholders to consider when the organisation is dealing with human resource issues, wages, working conditions or reductions in the size of its workforce. The formal power of unions has diminished in Australia over the past decade as a result of various industrial reforms, however depending on the industry or profession involved, they may still remain a significant stakeholder that can have a substantial influence on the operation and effectiveness of the organisation.

- *Expectations*: negotiating in good faith, member's rights such as workplace health and safety, awards and contracts, enterprise agreements, industrial action
- *Context*: production
- *Active/passive*: switch

Stakeholder analysis: assessing the needs of the stakeholder groups

Stakeholder analysis is one method of addressing the needs and wants of the stakeholders whilst meeting the organisation's objectives and goals. In the ideal scenario, the goals of the organisation will fit well with the needs of the key stakeholders, and minimise any potential conflict. In the worst case scenario, stakeholder analysis will provide an excellent starting point for a recovery strategy as the organisation attempts to address the gap between organisational goals and objectives, and the needs of the key stakeholders.

A process of stakeholder analysis

Stakeholder analysis, like much of business theory, is operationalised using a variety of methods, mechanisms and approaches. The method presented here is based on integrating the previous model of stakeholder impact with potential methods for assessing stakeholder needs. As with all strategy models, the value of the model is in the process of application, rather than assuming it will provide a fixed outcome. There are eleven steps involved in the stakeholder analysis process outlined below. These include:

1. Identify the stakeholder by name, key characteristic or other defining factor.
2. Identify if the stakeholder is passive or active.
3. Specify what the stakeholder wants from the organisation.
4. Determine the power dynamic in the relationship by specifying what the stakeholder will give in relation to what they want, and the discrepancy between the two levels.
5. Determine the level of urgency of the stakeholders' needs.
6. Group stakeholders by similar needs, constraints, wants, urgency or power ratios.
7. Analyse the possible developments that could alter the stakeholder situation either by increasing or decreasing the power and urgency of the stakeholder.
8. Determine how relationships with the stakeholder groups can be maintained, improved, built or terminated, as appropriate.
9. Determine the resources required to meet the needs of the stakeholders against the organisation's available resources.
10. Prioritise the stakeholders on the basis of the balance between the stakeholder analysis and the organisational objectives.
11. Develop and execute initiatives to deal with the stakeholders' needs and preferences according to their priority.

This framework has been derived from materials contained within Best (2005), Clement (2005), Doyle (2002), Freeman (1984), Frooman (1999), Grimble and Wellard (1997), Hooley, Saunders and Piercy (2004), Mitchell, Agle and Wood (1997), Neville, Menguc and Bell (2003), Proctor (2000), Scholem and Stewart (2002), Viljoen and Dann (2003) and Whitwell, Lukas and Doyle (2003).

1. Identify the stakeholder(s)

In this initial step make use of existing stakeholder analysis categories such as 'government' where possible, or specify exact groups (e.g. instead of 'unions' specify which unions are involved). For example, when dealing with the union stakeholder issues in a manufacturing business, it could involve the Australian Manufacturing Workers Union (shop floor staff) and the Australian Services Union (clerical and administrative positions). Scholem and Stewart's (2002) broad stakeholder map, along with the stakeholder categories of Table 3.2, can be used as a starting point. When first approaching a stakeholder analysis, this step can result in a considerable list of stakeholders, some of whom may be clustered together in the later steps of the process. At this point, key stakeholders are defined by their individual names (e.g. Esanda, GE Finance, Suncorp and Commonwealth Bank). Subsequent refinement during the analysis process will cluster the stakeholders into one or more categories (in the current example, Suncorp and Esanda are both members of shareholders and creditors, whereas GE Finance is just a creditor, and Commonwealth Bank is both a supplier and competitor). The identification of stakeholders is a complex and time consuming task when first undertaken, however, subsequent analyses can make use of previous stakeholder maps as a starting point. As with much of marketing, building on organisational knowledge and history is a key to reducing the amount of time which must be invested in the process, and to ensure that each marketing process is not reinventing the wheel (or running the same wheel concept past the same wheel focus group).

2. Identify if the stakeholder is passive or active

The second step is to determine if the stakeholder is active or passive, since this will determine the flow of influence between the stakeholder and the organisation. Using Grimble and Wellard's (1997) definitions, passive stakeholders are influenced by the organisation's actions, and active stakeholders exert an influence over the organisation's activities. Passive stakeholders tend to include the environment function, and may include the consumption function in transactional relationships. Active stakeholders include those in the production function, and those consumers in an ongoing marketing relationship that features co-production or customised products. For example, employees, managers and shareholders are active in influencing the decisions of the firm.

Finally, the switch stakeholders should be examined to see if they are passive/active for the particular situation of the analysis. For example, a respected lobby group may be active due to membership of a steering or advisory committee on a particular issue but passive for other issues concerning the organisation. Similarly, competitors can be deemed switch stakeholders, since they are influenced by the organisation's actions, yet have an equal ability to influence the organisation.

3. Specify what the stakeholder wants from the organisation

Having identified and created the stakeholder map, Step 3 requires the firm to create the stakeholder issues map, which is usually the hardest part of the process. There are no hard and fast rules for identifying the needs, issues, problems and opportunities presented by the stakeholders (Scholem & Stewart 2002). This is where the marketing manager needs to make use of existing organisational knowledge, such as:

- market research (consumer needs)
- existing business strategies (e.g. long-term value maximisation for shareholder, short-term profit seeking to repay creditors)
- business relationships (suppliers want ongoing sales, retailers/distributors want saleable products).

This is one of the most variable factors in a stakeholder analysis, and is based entirely on the specific organisation and its relationship with the marketplace at the time of the analysis.

4. Determine the power dynamic

Step 4 involves the use of the power–urgency–legitimacy frameworks outlined earlier in this chapter. Determining the power dynamic in the relationship between the organisation and the stakeholder is done by specifying what the stakeholder will give (support, money, regulation) in relation to what they want (design changes, useful product, less hazardous environment), and clarifying the discrepancy between what will be given, and what will be received.

For example, an environmental lobby group may give its open support to an organisation in exchange for that organisation altering its production processes to use environmental friendly processes. Alternatively, the lobby group could use its share of voice and power to pressure the organisation to change, where in exchange for conceding to the demands, the lobby group will cease its activity. In the first case, the exchange is relatively equal (endorsement exchanged for process changes), whereas the second case is an unequal exchange (cessation of wielding power in return for a process change).

Power is also determined by the level to which the organisation can resist the will of the stakeholder, either through countermeasures or the stakeholder not having sufficient influence to damage the organisation. Although portrayed here as a defensive strategy, resistance to stakeholder influence is part of the process of balancing the needs of production, consumption and environment. Whilst the stakeholders involved in the social environment may seek to leverage their power to change the nature of a product (e.g. religious lobby groups trying to reduce the spread of supernatural content in books), meeting the needs of the consumption group (purchasers of Harry Potter books) will mean resisting the power of the lobby group.

5. Determine the level of urgency of the stakeholder's needs

Step 5 builds on the previous framework of power and legitimacy by examining the urgency of the individual stakeholder's needs using frameworks such as Neville, Menguc

and Bell's (2003) model in Figure 3.4. The key aspect for prioritising stakeholders is the urgency of their needs given the available resources of the organisation, and the speed with which the need can be met. This can be used as a defensive measure where needs are met on the basis of a sliding scale from 'crisis' to 'heading towards crisis' to 'will wait until it's a crisis'. Alternatively, urgency can be used proactively as part of a longer-term strategic planning process to deal with high priority, high urgency tasks first, and then allocate resources to address the less urgent stakeholder needs over time. As mentioned previously, urgency is one of the most common determinants of stakeholder influence.

6. Group stakeholders by similar needs, constraints, wants, urgency or power ratios

Step 6 in the process requires the marketing manager to combine the various stakeholder groups into workable clusters for the development of strategies, initiatives and other business actions. In Step 1 of the process, the purpose was to identify all possible stakeholder groups, and individual stakeholders within those groups. Now, the requirement is to take that initial analysis and merge it into clusters, which can be based around a range of possible factors such as:

- shared needs
- similar levels of urgency
- common wants
- the relevant levels of power and influence.

This step is where diagrams such as Mitchell, Agle and Wood's (1997) model in Figure 3.2 and Figure 3.3 are useful for visualising the process, and determining clusters of shared characteristics (e.g. dependent stakeholders will have similar levels of power, and may also have other shared characteristics: employees, unions and managers may have similar needs whilst shareholders, creditors and financiers may have compatible levels of urgency, or the media and lobby groups hold similar levels of influence and power). Grouping the stakeholders is a subjective process based on the specific details of the situation, and the specifics of the stakeholders themselves.

7. Analyse the possible developments which could alter the stakeholder situation

Step 7 involves analysing the possible developments that could alter the stakeholder situation to allow the organisation to step back from the immediate moment and assess the longevity of the impact of the stakeholders. This ensures that decisions made to address the impact of the stakeholders also consider the longer-term picture. This approach uses the theoretical framework of Figure 3.3 to consider how shifts in power, urgency or legitimacy could alter the type and nature of the stakeholder (Mitchell, Agle & Wood 1997).

While a key stakeholder may have immediate urgency and power, if this power is likely to dissipate in the near future, it may be strategically more viable to resist the stakeholder's influence even if this means sustaining short-term losses for medium- to long-term gain. Similarly, a non-urgent, non-powerful stakeholder who has the potential to gain significant

power in the foreseeable future (e.g. opposition parties in government, populist lobby groups) may be best dealt with in the shorter term whilst they are in a weaker relative position, rather than waiting for them to become a significant influence (or threat).

8. Managing relationships with the stakeholder groups

Step 8 is to take a proactive approach to the stakeholder group, and engaging in managing the relationship with the stakeholder. This is the first step in the process that does not consist largely of information gathering and analysis. Stakeholder relationship management in this phase also integrates with the marketing concept where the management of the relationship is performed to create benefit for the stakeholder. This is where the information gathered on what the stakeholder wants (Step 3) is translated into what the organisation is prepared to offer. Management of the stakeholder relationship is based around four alternative positions:

- *creating a relationship with a stakeholder in order to address that stakeholder's specific needs*. This is used where the organisation has no existing relationship with a stakeholder, for example, Woolworths would be advised to create a relationship with the local community to receive its support for a new shopping centre, rather than to engage in a confrontational approach.
- *maintaining the relationship where it is adequately servicing the organisation and stakeholder's needs*. This approach presumes the existence of an ongoing relationship with the stakeholder. Satisfactory stakeholder relationships can arise from aspects such as long-term contracts (supply/distributor stakeholders), and as such would not need to be created from scratch, but rather maintained and refined over time.
- *improving the relationship where it is not meeting the needs of the organisation and/or the stakeholder*. If the stakeholder needs are not being addressed successfully, and this is a key stakeholder group, the relationship will need to be improved. At the same time, a stakeholder relationship that is detrimental to the organisation also needs to be improved. This option should also be examined in light of Step 7, which is the assessment of how the stakeholder relationship could alter—for example, an average relationship may turn hostile if market conditions change.
- *terminate the relationship with the stakeholder where it is no longer needed*. Termination of the relationship occurs when the stakeholder group no longer has an issue, involvement or opportunity with the organisation. For example, a firm that has divested itself of manufacturing plants will no longer require a relationship with the Australian Manufacturing Workers Union. Termination of the relationship only occurs where there is no further interaction between the stakeholder and the organisation—not where the stakeholder and the organisation have a poor relationship. For example, Greenpeace and Shell still have a stakeholder relationship, even if it is one of conflict. If Greenpeace leaves the environmental stewardship industry or Shell stops being Shell then the relationship may be able to be terminated.

Again, because of the variable nature of the relationship between organisation and stakeholder, there are no hard and fast rules on how best to engage in this process. However, much of the fundamental theory and practice of relationship marketing will be useful in this context; particularly issues such as commitment, trust and reciprocity, which impact on the success of a relationship (Chapter 1).

9. Determine the resources required to meet the needs of the stakeholder against the organisation's available resources

Step 9 is the direct follow-on from deciding to engage, maintain or upgrade the relationship by determining what resources to spend to perform that task. Resource allocation can be merged with the previous step in the process where strategies were being set and created to meet each stakeholder's requirements. However, for the most part, resource allocation tends to be controlled outside of the marketing strategy area, and as such tends to be uncovered after the setting of broad based strategy. That said, the financial and production aspects of the internal analysis covered in Chapter 4 will assist in maintaining an awareness of the resources available to manage the stakeholder relationship. With this insight, appropriate marketing strategies can be developed around the estimated available resources in order to maximise the likelihood of the approach becoming reality. In other words, don't plan to create a resource intensive relationship unless you have those resources at your disposal.

10. Prioritise the stakeholders on the basis of the analysis and the organisational objectives

The tenth step is the determination of the priority order of the stakeholders. In theory, there is a range of approaches to take to handling the prioritisation, and many of those were covered earlier in the chapter. In reality, priority is usually determined by perceived urgency, and urgency with power usually wins out over legitimacy or power alone. In addition to simply just dealing with the most urgent stakeholder needs, and planning a relationship around addressing that immediate situation, marketers can also plan longer-term relationships based on the analysis just completed and objectives of the organisation. (Organisational objectives will be covered in Chapter 6, and the specific aspects of organisational objectives and stakeholder relationships will also be addressed in Chapter 14 and 15.)

11. Develop and execute initiatives to deal with the stakeholders' needs and preferences according to their priority

The final step in the process is to actually manage the relationship with the stakeholders. Many strategic marketing models skip the final step, which includes developing the appropriate plans of action, making the requisite changes to the organisation's activities, and including the prioritised stakeholders' needs and wants in the day-to-day running of the organisation. Failure to act on the stakeholder analysis invalidates the entire process, and wastes the resources of the organisation that were spent on the analysis process. Although an apparent statement of the obvious, it serves as a reminder that whilst analyses and the analysis process are equally important, they are both irrelevant without the implementation of outcomes into the activities of the organisation (Chapter 15).

Stakeholder interaction

For the most part, this chapter has presented stakeholders as independent units of analysis and discussed and dissected them as individual components. Whilst this is useful when examining conceptual models, it is important to remember that in business, the stakeholders will be interacting with each other in a dynamic environment. The most complicated method of viewing the interaction is to consider that each group of stakeholders has its own set of stakeholder groups. Consequently, whilst the media may have power over the organisation, the media itself is influenced by the government, which is influenced by unions, who are influenced by their members, who are influenced by their local communities and so forth. Consequently, addressing stakeholder needs will result in trade-offs between the different stakeholders, who in turn are readjusting their own position in reaction to their stakeholders. Whilst not as bad as chaos theory for demonstrating interactions in a complex system, remembering that stakeholders are interconnected parts of the business environment can avoid the error of assuming marketing strategies targeted at one stakeholder group will not impact on non-targeted groups.

Upstream stakeholder interaction

One aspect to consider when addressing stakeholder needs is whether the needs of one stakeholder can be influenced by 'upstream' marketing. Goldberg (1995) defined upstream marketing as manipulating the environmental variables, market conditions and market needs by targeting the level above the consumer, rather than consumer directly. Instead of creating primary demand for the product to expand market share, the upstream marketer improves conditions for the market to expand overall, thus increasing the available customer base. For example, downstream marketing focuses on selling more products to customers (e.g. larger units of popcorn in cinemas), whereas upstream marketing encourages cinema owners to run more movie sessions, and film makers to produce shorter films to increase the potential number of popcorn purchasers in a given time period. Upstream marketing in the stakeholder context can involve lobbying governments, unions and media either to reduce the share of voice possible for lobby group stakeholders or to increase the power and urgency dynamic the organisation has with its stakeholders.

Working with stakeholders

Stakeholders should not be automatically considered opponents by an organisation. Instead, the organisation should look to maximise the benefit for both itself and its stakeholders by working with the various groups where possible. Viljoen and Dann (2003) propose eight points for working with stakeholders:

- *Find common ground*. Stakeholders can become allies, or at least neutral where both the organisation and the stakeholder share a mutual interest in an outcome.
- *Involve the stakeholder early*. As mentioned above in 'Urgency', involving stakeholders before they become urgent or crisis-level priorities should be part of the organisational strategy.

- *Be prepared to compromise*. Compromise positions are the balance between the wants and needs of the stakeholder and of the organisation, and as such, represent the *quid pro quo* exchange between the two groups.
- *Be consistent and stick to key principles*. In many cases, the wants of the stakeholder far exceed what the organisation can give without suffering significant loss or impossible working conditions. Similarly though, the organisation's wants can be equally impossible for the stakeholder. Establishing base line core principles that the organisation will not move from during the give and take process with the stakeholders assists in developing a balanced or compromise position. In addition, the stakeholder is likely to have a core set of values which will remain consistent.
- *Spell out the benefits of the organisation's position*. Communicate with the stakeholders and explain the organisation's goals, objectives, and the positive impact of the organisation's objectives on the stakeholder. This is particularly important where the passive stakeholder has the potential to become an influential active stakeholder. Explaining the benefits of the organisation's position may persuade them to remain passive stakeholders.
- *Explain the 'big picture' in terms of the longer-term benefits and broad impact of proposals rather than the short-term micro issues*. Quite often a stakeholder can see an immediate negative impact on their needs, wants or lifestyle, but is not able to see how the action will lead to longer-term gain without the organisation explaining the details of the process and its effects.
- *Listen to the stakeholders*. Stakeholders can be valuable sources of competitive information, market knowledge and product information. If a stakeholder group has taken the time and effort to present a case to the organisation, it is worth listening to them in the first instance. For example, concerned citizen groups lobbying about product safety may actually present ideas for a viable product upgrade.
- *Involve the stakeholder in the decision making*. This has two effects that benefit the organisation. First, stakeholders who are involved in the decision process have a sense of ownership of the decision, and can assist in the defence of that position alongside the organisation. Second, and highly cynically, stakeholders who have a record of criticising the organisation lose credibility, legitimacy and power when they are part of the decision making process that created the problem they are now complaining about. Getting 'buy in' to the decision process can also assist in getting 'sell out' from stakeholders prone to opposing to the organisation.

Many of the principles of dealing with stakeholders are derived from relationship marketing. Concepts such as 'Sticking to the facts' are related to the issue of trust. Similarly, the willingness to compromise is parallel to the reciprocity notion of the marketing relationship. One of the core values implicit in the stakeholder analysis, stakeholder process and working effectively with stakeholders has been the common thread of both treating the stakeholder with respect and recognising that the stakeholder is an active participant in the process.

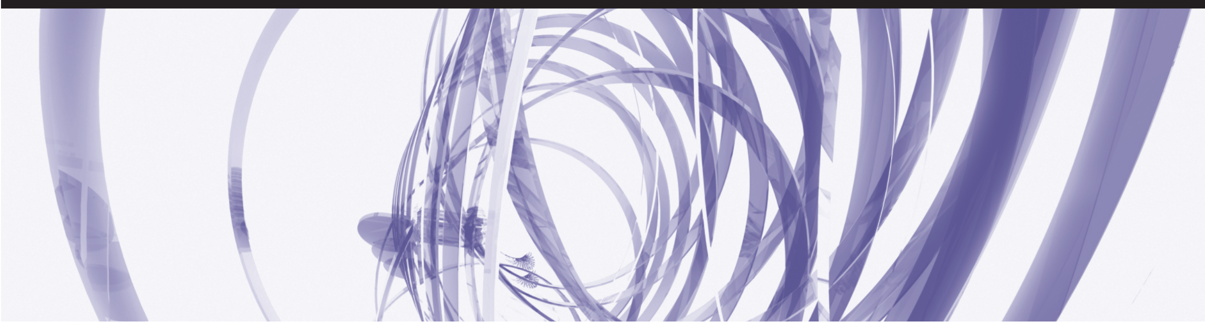
Conclusion

The explicit inclusion of the importance of stakeholders into the revised formal definition of marketing means that marketing strategists now have to pay far more attention to how their proposed strategies will impact on, and be influenced by, a far wider range of forces than in the past. While these influences have always existed, the progression of the marketing function away from a managerialist perspective and towards a higher-level strategic view means that thorough stakeholder analysis is essential before developing a marketing strategy, rather than leaving this activity to broader-based corporate strategists.

In analysing stakeholders and their likely influence on marketing strategy development, three criteria need to be taken into consideration: power, legitimacy and urgency. Depending on the situation, a stakeholder may be active in their reaction to the organisation's strategy and sufficiently powerful to require a response. However that same stakeholder may lack both power and sufficient interest in other strategies to react and elicit a response. As in all areas of strategy, the relative importance of different stakeholders will vary according to situation and there are no hard and fast rules as to which one(s) should be the focus of sustained attention.

Analysis 1—Internal analysis

CHAPTER 4



Framework for internal analysis of the company

The internal analysis of the organisation is the first of the purely analytical phases to be considered in this book, but can often be the second or even third phase in setting the marketing strategy. The problem with competitive strategic marketing is that there is no real 'right' or 'wrong' method for determining whether to conduct the internal analysis first to determine the strengths and weakness of the organisation, or whether to examine the external influences of the market and environment to determine opportunities available to the organisation and then review organisational capacity to capitalise on these opportunities. It is even possible to set objectives first, review market conditions second and assess organisational capabilities to determine how to achieve the preset goals. For the purposes of this book, internal analysis will be examined first to build on the previous chapters on strategic models and stakeholder selection. However, in business, it may be necessary or advantageous to work from the external analysis.

This chapter covers four major areas based around the elements of the Kaplan and Norton (1996) 'balanced scorecard'. In addition, it draws on several of the models raised in Chapter 2, along with introducing new concepts and models such as shareholder value analysis. Whilst the book will recommend areas to analyse, and suggested types of techniques, it will not include the implementation level issues of performing the analysis, due to the focus of the text being at the strategic rather than tactical level.

Balanced scorecard approach

Kaplan and Norton (1996) introduced the concept of the balanced scorecard which represents a movement away from the traditional focus on financial returns to a four-way strategy that recognises there are more issues leading to long-term success in business than per-unit profit. Although Kaplan and Norton applied the initial balanced scorecard process to the strategic business unit, the fundamental principles of balancing financial issues against customer relationships, internal business issues and organisational innovation can be applied at any level of the business.

Four elements of the balanced scorecard

Kaplan and Norton (1996) defined the four areas that needed to be balanced as:

- *financial*, which covers the return on investment and economic value added aspects of the organisation. This incorporates the need to manage marketing relationships for the benefit of the firm, as well as the customer and stakeholders. The financial element of the scorecard is usually of most interest to the stakeholder groups such as the board, creditors, financiers and shareholders.
- *customer relationships*, which include customer satisfaction and retention along with issues such as market share and account share. In addition, it encompasses the relationship management component of the 2004 definition of marketing, and the consumption context of the stakeholder analysis, making the customer the primary stakeholder interested in this area.
- *internal business issues*, which incorporate the business operations and issues such product quality, production response time, and the development and introduction of new products to the market. This part of the scorecard covers the production context of the shareholder value analysis and stakeholder analysis. This incorporates the stakeholder groups of employees, management, distributors, suppliers and shareholders. The internal business issues section also incorporates models such the Directional Policy Matrixes from Chapter 2, organisational resources, portfolio analysis and related models.
- *innovation*, which encompasses the learning and growth capacity of the firm, employee satisfaction and the use of information systems and knowledge management. Innovation in this context is the intra-organisational capacity to develop new ideas and evolve operational processes as a result of organisational experience. This incorporates aspects of the production context including stakeholder issues for managers and employees involved in the organisational learning process.

The principle of the balanced scorecard is that an organisation needs to diversify its objectives and focus to ensure it balances the need for financial gain (profit), against the need to service the customer (to make the sales that lead to financial gain), against

the internal business issues (such as producing quality product to sell), against the need to innovate and grow the capacity of the firm (employee satisfaction or new business processes).

Balanced scorecard v. triple bottom line

The balanced scorecard has a market competitor in the form of the 'triple bottom line' concept. The triple bottom line evaluates an organisation on the basis of economic, environmental and social accountability. In essence, what the triple bottom line model does is emphasise the need to balance the needs of the customer and the organisation against the needs of the stakeholders. For the triple bottom line, key stakeholders are environmental lobby groups (environment), local and broader community stakeholders, and those social pressure groups that deal with the relevant social issues being measured under social accountability (e.g. disability access for service providers or equal opportunity employment). For this text, the triple bottom line of economics, environment and social accountability is merged into the stakeholder benefit and the balanced scorecard approaches, since the key elements of all three areas overlap. If a firm is unbalanced in one aspect of the triple bottom line (e.g. overemphasis on social issues), it will become apparent in the balanced scorecard (underemphasis in financial analysis and objectives) or the stakeholder analysis (lack of attention to shareholder, customer, financiers, creditors and/or board of directors). In addition, the triple bottom line's external focus on environmental impact and social accountability reduces its value for internal analysis compared to the balanced scorecard.

Balanced scorecard element 1: financial analysis

For the organisation, the first and foremost focus of analysis is financial. Whilst many of the issues raised in the remaining three parts of the scorecard are important, they all depend heavily on the financial wellbeing of the organisation. At the end of the day, businesses exist for the purposes of generating a financial return to ensure the ongoing survival of the organisation and continued capacity to meet the customer's needs. In an optimal arrangement, the organisation can continue to survive financially whilst acting responsibly towards customers, employees, the environment and society.

Issues in financial analysis

As this is a competitive marketing strategy book, the emphasis of this chapter is on marketing rather than financial strategies. However, marketers should at least familiarise themselves with the basic financial analysis skills to be able to work with the specialised finance or accounting divisions of the organisation. In addition, the parts of the firm responsible for controlling budgets, recording income and monitoring expenditure should be treated as allies in the marketing process. The purpose of marketing, and marketing strategy, is to benefit the customer, the organisation and the stakeholder. Organisational benefit at the most basic level is financial return, and as such remains the number one

long-term outcome of the marketing process. Consequently, the marketing financial analysis should concentrate on the following areas:

- demonstrating the return on investment ratio between marketing activity and sales revenue
- making use of any available marketing metric to demonstrate the impact of the financial investment in the marketing campaign
- engaging in internal marketing to demonstrate that marketing activities are investments to be made in revenue generation, rather than costs to be cut when budgets are under pressure.

Defending the spending

For the marketing strategist, one of the most important factors in the financial analysis process is to show the cost of alternative marketing strategy selections, and justify why these costs would have led to reduced revenue level. Alternatively, the analysis should be used to demonstrate that the chosen strategy was the optimum use of the organisation's money. For example, television advertising is a high-impact and high-cost technique which, when compared to print media, may be considered a waste of the organisation's budget. However, when the higher cost investment will bring about the better return (e.g. print advertising can't convey the sense of emotion needed to sell the product), selecting the lower cost alternative may lead to reduced sales revenue, which ultimately reduces the financial success of the organisation.

Production context stakeholders: financial context

The financial analysis arm of the balanced scorecard will be of most interest to the financier, creditor and shareholder stakeholders, all of whom have a direct financial interest in the organisation. In particular, militant shareholders are more likely to be scrutinising the marketing expenditure looking for 'waste' in areas such as corporate entertaining, sponsorship or expensive advertising. In order to meet the needs of the stakeholders in this regard, marketing strategists need to justify and defend the investment by tying the financial analysis (sales revenues from investment costs) to the organisational objectives in customer relationships, strategic objectives and stakeholder benefit. For the most part, any stakeholder with a financial interest in an organisation wants to feel that they are receiving the maximum benefit for their investment. Marketing metrics tied to financial analysis and organisation goals can show that strategic options taken by the firm are attempting to maximise that gain, and address that stakeholder issue.

Balanced scorecard element 2: customer relationships analysis

The second element in the balanced scorecard is customer relationships, which is the balance between serving the needs of the customer and maximising the benefit for the organisation and its stakeholders. Doyle (2002) raises the issue of the disequilibrium between different organisational objectives and stakeholder benefits, particularly the split

between shareholder value and customer value. Customers usually want to purchase the product at the lowest possible price whereas shareholders want the higher prices set in order to maximise profit. In essence, the disparity between organisational wants and customer wants in a dynamic marketplace leads to a need to balance the two areas, and use factors such as brand loyalty to increase the customer's willingness to purchase the product at higher margins, thus increasing shareholder value.

Recognising the consumer as a player in the consumption game

In Chapter 1, Carson, Gilmore and MacLaran's (1998) six-step model of the philosophy of marketing included reference to the need to respect the consumer as an active and informed participant in the marketing process. The first priority of the customer relationship analysis in the balanced scorecard approach is to assess the level of respect shown to the customer, and what level of recognition of their involvement is expressed in the marketing strategies. Consumers should not be perceived as resources to be harvested, but rather, as active participants in the consumption process. Whilst the organisation is competing for the attention of the consumer, the consumer is also playing the organisation off against its competitors to maximise the benefit that the consumer can receive.

Consumption context: consumer as stakeholder

Consumers hold an odd place in the stakeholder analysis as direct beneficiaries of the marketing actions of the organisation, and indirect beneficiaries as stakeholders. Broadly, as consumers, they have their needs and wants met by the product offering. As stakeholders, they also want full disclosure on risks, safety issues, product recalls and/or other information that impacts on the use of the product and that may arise from previous use. For example, whilst the consumption need is for a solution to morning sickness in pregnancy, the stakeholder need is for disclosure of side effects, possible long-term effects of product use, and a reasonable expectation that the product is safe for mother and child. This mixture of stakeholder issue and market need must be kept in mind when dealing with the customer. To further complicate matters, consumers can also be individual members of other stakeholder groups (e.g. local community, employee) or influence the organisation in other contexts (e.g. government as regulator whilst also being a potential customer).

Core customer outcome measures

Unlike the volumes of financial analysis options available to business, there are fewer clear-cut metrics and measures to determine the customer analysis. Some of the more common measures include:

- *satisfaction*, which is the level to which the organisation is meeting the customer's needs
- *loyalty*, which is the intention of the customer to remain with the organisation, or to continue using the organisation's products to satisfy their needs

- *retention*, which is the level of success in maintaining the customer, and includes the costs of loyalty schemes
- *acquisition*, which is the process of acquiring the customer, and the costs associated with the marketing required to either cause new product adoption or brand switching so that the customer uses the organisation's product
- *profitability*, which is the difference between the revenue earned by the customer, both directly and through referrals, and the costs incurred in retaining the customer.

These are examined in greater detail below.

Satisfaction

Satisfaction is a major driver of customer retention and customer loyalty. Whilst some customers are purely price driven, most will base their purchase decision on the level to which the product satisfies their needs. Consequently, the analysis of satisfaction should focus on:

- whether the firm is achieving an appropriate level of satisfaction
- whether this level can be raised
- whether altering the value offering to change the satisfaction will increase the cost, decrease the profit, or endanger the level of satisfaction experienced by other customers.

Satisfaction can be measured in a variety of ways, including:

- voluntary market feedback such as unsolicited comments given to the organisation's staff
- customer surveys, exit surveys or after-sales follow-up calls conducted as part of an ongoing satisfaction measurement plan
- market research surveys conducted either internally or by external consultants to examine self-reported levels of satisfaction
- monitoring online discussion forums related to the product or service, either those hosted on the organisation's own website or through the use of web search, keyword searching for the organisation and other online research techniques.

Doyle's (2002) disequilibrium concept also applies to customer satisfaction since the value offering is likely to only meet a portion of the client's needs. Consequently, due caution should be taken to see that modifications to product offering to increase one customer group's satisfaction does not reduce the satisfaction level of other profitable groups. For example, potential customers of a gym may desire aerobic walking machines, whereas the current customers prefer weightlifting equipment. Altering the number of machines of a certain type (increasing walking machines) will result in the reduction of equipment (weights) used by more regular members. The gym management would need to ensure that they balanced the satisfaction of the regular (and profitable) members when they considered altering the product offering to entice the non-members.

Loyalty

Loyalty is the propensity of the customer to select the organisation's value offer ahead of alternative offers from competitor organisations. In addition, loyalty also represents the organisation's propensity to reward the consumer's continued choice with special offers, discounts or other value additions based on the level of loyalty. It is predicated on the assumption that the lifetime value of a regular customer is greater than the costs of retaining that customer or the costs of acquiring new customers.

Loyalty is a dyadic commitment between the organisation and the customer, and as such should be measured carefully to ensure that the customer wants to engage in an ongoing relationship and that when they do, they are going to receive a benefit for being loyal. Customers who are satisfied with transactional relationships may not want to engage in loyalty schemes, and can even have their satisfaction reduced by being forced into loyalty programs that they feel are only designed to benefit the sponsor organisation. Loyalty can be measured through:

- use of loyalty programs such as vouchers, special pricing incentives for loyalty card holders, or uptake on product offers
- database marketing, including the data collected from reward cards, reward programs or online sales tracking
- the duration of the customer's dealings with the firm, e.g. more loyal customers stay with the organisation for longer
- measuring volume of purchases over time, with the assumption that loyal customers maintain or increase their purchase volume
- market research conducted on the customer database by a third-party research organisation.

Retention

Retention is separate from loyalty in that it represents repeat transactional purchases, or ongoing purchasing behaviour that is not part of a loyalty scheme. Consumers who consistently select the organisation to meet the needs, but are still willing to select competitor offerings when they are cheaper, more easily accessible or provide an additional benefit are still customers of the organisation. With the increasing emphasis on relationship marketing it is easy to overlook the role of non-loyalty based customer retention. Providing products in transaction at a profit over time is still a viable business strategy. The decision to undertake a series of repeated purchases over time from a particular supplier does not necessarily indicate that the individual or organisation wants to engage in a 'marketing relationship'.

Retention is measured in terms of sales, both ongoing contracts and repeat purchases. Without the benefit of the loyalty programs of relationship marketing, it can be more difficult to track retention to individual purchasers. Repeat sales are an adequate measure of customer retention, although it can also be measured by increased sales volumes from non-loyalty based repeat customers.

Acquisition

Acquisition is the process of taking a new customer through the marketing process from awareness of a need through to using the organisation's product to satisfy that need. In the internal analysis, it plays the role of measuring the cost of gaining a new customer, so that relationship strategies can be budgeted in the context of the cost of retaining customers versus the cost of acquiring new ones. Acquisition costs also become an important issue when planning growth strategies based on product development (new products, new consumers) or market development (new consumers, current products). Acquisition costs can be measured as a function of the marketing expenditure divided by the number of new customers (transactional or loyal) acquired over a specified time period.

Profitability

Whilst satisfaction is the lifeblood of the customer's continued desire to transact with the organisation, profitability is the basis on which an organisation judges whether it wants to serve that customer's needs. In many respects, profitability is an objective measure of the organisation's satisfaction with the relationship with the customer. This aspect also ties back to the financial analysis, and is heavily dependent on factors such as:

- the lifetime value of the customer which includes measuring the costs of retaining the customer against the revenue generated by that customer over time
- acquisition costs and customer revenue per transaction for new, non-loyal, or transactional customers
- costs of servicing the customer after the transaction, e.g. warranties, service calls and the costs of satisfaction tracking
- costs of maintaining the organisational infrastructure, running costs, organisational overhead, salaries and other costs per product versus the revenue raised by the product.

Customer profitability is calculated as the net difference between the costs spent and the revenue earned from the customer. It is present in the internal analysis to assess the value the customer represents to the organisation at the same time as the organisation is reviewing what value it delivers to the customer.

Value proposition analysis

Kaplan and Norton (1996) introduced value proposition analysis into the scorecard's measurement of customer relationships to assess what benefits the organisation was delivering to the customer. Value was taken to represent the attributes that organisations provide to their customers, which were then expressed as the sum of the product or service's attributes, the customer's perception of the value of relationship with the organisation and the organisation's image. This is assessed by Kaplan and Norton's value proposition equation:

$$\text{Value} = \text{Product or service attributes} + \text{Image} + \text{Relationship}$$

Product or service attributes

The first element of the value proposition is the capacity of the organisation's product or service to meet a customer's need or want. This is the most basic aspect of the marketing process, and without it, there will be no customer satisfaction, loyalty or even transaction. In general terms, the product/service attributes are defined by elements such as:

- *functionality*, which is the extent to which the product actually performs the task required to meet the needs
- *quality*, which is the subjective level of satisfaction with the intangible elements of the performance, and the worth or value level of the component elements of the product. For example, whilst a communications need can be solved by a high gloss brochure or a photocopied note, the quality of the paper can impact on the client's satisfaction with how the need was met
- *time*, which incorporates the amount of effort, energy and forgone opportunities required for the need to be satisfied by the organisation's product
- *price*, which represents the financial price of the product and the non-financial costs of social influence, e.g. loss of pride if ownership of the product causes embarrassment.

Analysis of the time costs, financial costs, intangible quality of the product and the extent to which it performs the desired purpose can be conducted either through market research with the customer or internal review of the production processes.

Image and reputation

The second part of the value proposition is the intangible factors such as perceived quality, reputation and other factors that draw a customer to a company. These factors can be influenced by integrated marketing communications, branding strategies and positioning strategies. For example, the branding of bottled water allows for considerable price variations based on the image associated with the organisation behind the brand.

The analysis can be conducted by an image audit, market research with customers and non-customers and through secondary sources such as content analysis of reviews of the product or organisation. The image and reputation component of the value proposition is extremely subjective, and as such is often difficult for the customer to convey, or the market researcher to capture. However, given that strategies such as brand leadership rely heavily on reputation in the value proposition, it is an important aspect to consider.

Customer relationship

The third component of the value proposition is the balance between the type of relationship the customer wants, and the type of relationship the firm is willing to provide. This includes factors such as:

- the actual delivery of the product
- after-sales service
- how the customer feels about buying from the organisation.

This factor is integral to the loyalty and retention elements mentioned above, and contributes heavily to satisfaction with the product. Customers with a poor relationship with a firm will often forgo a superior product in favour of a less adequate solution from a less disliked provider. Analysis can include the use of mystery shopper tests to see if the product is delivered as promised, market research and monitoring of the transaction ('this call may be recorded for quality checking purposes') to ensure that delivery is to the preset standards.

Balanced scorecard element 3: internal business issues analysis

Internal business analysis refers to the introspective focus on the capacity of the organisation. This form of analysis relates to the business competitive position elements of the GE/McKinsey Directional Policy Matrix Variant covered in Chapter 2. This section covers five different analysis models, which include:

- shareholder value analysis
- assessment of organisational resources
- portfolio analysis
- core competency analysis
- Porter's Value Chain.

In addition, it addresses the role of the employee, and the need to assess employee satisfaction levels as part of the internal analysis process.

Analysis I: shareholder value

Shareholder value is based on the principle that the primary goal of the organisation is to deliver value to the shareholders by maximising the financial returns on their investment (Doyle 2000). Shareholder value can be seen as an organisational philosophy, which in turn is represented by a three level construct of:

- *beliefs*, which encompass the acceptance that maximising shareholder benefit is the primary goal of the organisation
- *principles*, which are the strategic foundations used for determining value, and which include targeting profitable markets and the creation of a competitive advantage that gives value to the customer and the organisation
- *processes*, which are the activities undertaken to implement the beliefs and principles and include the development of strategy, allocation of resources and evaluation of performance.

Shareholder value is improved through dividends, increases in the value of the shares and cash payments. In theory, pure shareholder value maximisation strategy should lead to the company focusing on short-term financial gains that either pay cash directly to the shareholder, or improve the share price in the market. Consequently, the shareholder value model reinforces the presence of the disequilibrium pressures to balance the

stakeholder needs of the shareholders (maximised return) against the needs of other stakeholders such as the customer (value), employee (wages) or community (environmental protection). Placing the shareholder at the top of the food chain also impacts on the other stakeholders in the production process such as employees and unions where their interests of higher wages, job security and adequate reward for work performed can conflict with strategies aimed at increasing shareholder value by cutting costs and maximising profits.

Role of shareholder value

The role of shareholder value in the internal analysis is twofold. First, it should be used as a benchmarking measure to determine the state of shareholder value prior to the application of the marketing strategy. As with financial analysis, the information derived from the shareholder value analysis is designed to provide quantified, objective measures of the marketing strategy's impact.

Second, the calculation of shareholder value requires an examination of the financial aspects of the marketing, including the analysis of marketing assets, revenue per sale, marketing costs and cash flow calculations. Working on the assumption that marketing's role in the organisation is to create shareholder value then marketing investments, when applied correctly, should create assets that can be used to generate future cash flows.

Marketing assets in this context refers to:

- *marketing knowledge*, comprising assets such as the skills, systems and information used in identifying market opportunities and developing marketing strategies
- *brands*, which are the brand names, intangible reputation and image aspects of the firm that give value to the customer, and which drive the customer's desire to purchase from the firm
- *customer loyalty*, which is the extent to which the customer will stay with the firm, and the lifetime value of the customer
- *strategic relationships*, which are the company's network of contacts within the industry, access to distribution systems, new markets and avenues for incremental sales.

Components of shareholder value

To analyse shareholder value, it is first necessary to understand the component elements of the concept. Doyle (2000) outlines the determinants of shareholder value as:

- *cash*—the surplus money once costs have been covered
- *time value of the cash*—the increased value of cash held today versus cash held tomorrow
- *opportunity cost of capital*—the level of return the shareholder could receive elsewhere in a company of similar risk, nature and size
- *the net present value*—the value of an asset as the sum of free cash flows minus the opportunity cost of the capital.

This translates into the formula:

Net present value = Sum(Cash) – Opportunity cost

Doyle (2002) also outlines the following equation for representing cash flow:

Sum(Cash) = (Sales growth × Net operating margin) – Net investment

Cash is the difference between revenue (sales × profit margin per unit) and the costs (net investment). In this model, the most effective method for increasing cash flow, and therefore shareholder value, was to adjust the net operating margin. Increasing the net operating margin was seen as a factor of the strength of the organisational brand, customer loyalty and market willingness to tolerate an increase in price for the product. Consequently, a strong brand that is able to increase in price can return greater rewards in both short- and longer-term than cost-cutting measures. For those readers wishing to further examine the process of shareholder value calculations, Doyle (2000) illustrates several cases of the calculation of net present value, effects on future cash flow, and how to calculate the role of marketing in increasing shareholder value.

Analysis II: assessment of organisational resources

The second analysis is the assessment of the resources available to the organisation. This analysis forms part of the business's competitive position for use in the GE/McKinsey Directional Policy Matrix Variant. The emphasis of this analysis is on viewing the organisation in terms of what strengths, assets, capacities and capabilities it has available for use in the marketplace. Day's (1994) definition of resources as consisting of assets and capabilities will be used for this analysis. In Day's (1994) model, assets are divided into tangible and intangible components. However, assets only present one side of the resource picture. The second element is the organisation's business capability which is divided into the three areas of strategic, functional and operational capabilities. Those three areas then occur at the individual (employee), group (business unit) and corporate (organisational) level, creating a classic 3 × 3 matrix.

Types of organisational resource assets

Day's (1994) types of assets are:

- *physical assets*—the strictly tangible elements such as land and business facilities. In e-commerce orientated companies it may be possible to consider factors such as hard drive space, webhosting or other virtual environments as intangible assets
- *financial assets*—the tangible factors such as cash, and intangibles such as credit ratings or creditworthiness
- *operations assets*—including tangible elements such as plant and machinery for producing the product or service (e.g. the restaurant) and the intangible elements of systems and processes (the recipes and cooking techniques)

- *human assets*—the people employed by the firm (tangible) and their characteristics, personalities, skills, education and abilities (intangible)
- *marketing assets*—which are tangible elements such as the customer databases and the intangible aspects mentioned in shareholder value analysis (e.g. brand, customer loyalty, customer relationships, brand names)
- *legal assets*—in which the tangible elements are the patents and copyrights and the intangible element is the reputation of the legal department for being willing to pursue and enforce the legal rights held by the organisation
- *systems assets*—which are tangible aspects (e.g. knowledge management systems, databases) and intangible components of decision support mechanisms (including the organisational knowledge stored in the knowledge management systems).

Assets vary in the degree to which they can, and will, be reported in accounting and organisational reporting. Whilst obvious physical assets are counted on the spreadsheets, other assets such as employees may be recorded as costs (wages) or not recorded at all (brand position). The purpose of the resource analysis of assets is to determine what equipment, supplies, skills and raw materials are available to the organisation. From this base information, the organisation can elect to increase or improve an asset base, or it can be used as grounds to lessen interest in a market segment due to lack of resources.

Organisational resource capabilities I: strategic capability

Organisational capabilities are divided into component elements and, as such, consist of the interaction between the component part (e.g. ideology) and the three levels of employee, business unit and organisational level. Day (1994) outlines the strategic capabilities which set the direction for the firm as including:

- the dominant logic, ideology or orientation of the management (e.g. customer orientation, shareholder value orientation, production orientation)
- the ability of the organisation to learn, which can occur by acquiring, adapting or assimilating new information
- the ability of the management to manage the strategy implementation.

Strategic capabilities involve the stakeholders of management, board of directors and shareholders as drivers of the overall organisational agenda. At this point in the analysis, these drivers need to be recognised as they will be required knowledge for setting appropriate marketing strategies that coexist with the organisation's overall strategic direction.

Organisational resource capabilities II: functional capability

Functional capabilities refer to the ability of the firm to implement the strategy and tactics on a day to day basis and include:

- marketing capabilities, such as market research, PR, advertising, product development and management of customer relationships

- financial management, which includes the budgetary processes, billing cycles and other monetary controls
- operations management, which overviews and manages the operational capabilities (below).

Functional capabilities are influenced by management, employee, distributor and supplier stakeholders. In addition, financial management issues may also involve the creditor and financier stakeholders, particularly where the financier stakeholders request specific accounting measures or information regarding organisational finances for issues such as credit ratings. Factors such as the functional capacity of the organisation can influence the viability of the organisation's strategies for growth. For example, if the organisation is operating at peak capacity, growth strategies will require additional functional capacity.

Organisational resource capabilities III: operational capability

Operational capabilities are those areas involved in the actual value delivery of the product or service to the customer, and include:

- undertaking individual line tasks such as serving coffee to the customer, assembling component parts into the product and operating machinery;
- the application of information systems including filling out feedback forms, recording customer information, processing database forms and actually inputting organisational knowledge into the knowledge management systems
- the completion of order processing.

Operational capabilities are influenced by the production and consumption stakeholder context where the employee and customers interact in the delivery of the product or service. Analysis at this level involves assessing the delivery of the product or service to the customer, and factors such as the product quality, customer relationships with the organisation, and employee satisfaction. Again, as with the functional capabilities, these factors can determine the success or failure of a strategy. Whilst the management may see growth opportunity through market penetration, actually implementing an increased rate of customer turnover can only be achieved if the analysis of the functional and operational capacity has been undertaken to determine what capacity is available to the organisation to implement this strategy.

Analysis III: portfolio analysis

Business portfolio analysis is based on assessing the strategies for meeting customer needs through the range of products and services offered, both currently, and under current development. It is based on assessing whether the products offered by the firm are balanced in terms of cash flow, future prospects and risk. Products are divided into the broad categories of those that are currently generating cash, and those that are currently using cash but show potential to be cash earners later. Hooley, Saunders and Piercy (2004) outlined three possible portfolio types:

- *balanced portfolios*—in which products are generating cash now, and there is a pool of potential products under development which are using cash, but not in excess of the current income. This portfolio is a balance between present earning, risk on future earnings, and the risk of downturn in the current product offerings
- *unbalanced present-focused portfolios*—these are portfolios that are heavy with products currently generating cash, but lack future products or have limited new products in development. This type of portfolio is highly profitable under current market conditions, but vulnerable to shifts in the market. It has a high risk of the organisation suffering losses in the future if the cash-generating products decline before replacements are developed
- *unbalanced future-focused portfolios*—those portfolios that currently lack cash generating products to fund the new products which require cash investments in order to be developed for market release. Future-focused portfolios rely on the intervention of investors and financiers and present the high risk of the funding running out before the products become self-sufficient.

The portfolio analysis technique can be used for risk management or product and cash flow assessment, which can then be used in setting organisational objectives (Chapter 6).

Analysis IV: core competency analysis

Core competency analysis is a method for determining the central value proposition that is created, communicated and delivered to the customer. In this sense, core competencies are the fundamental basis for competitiveness insofar as the competencies represent the absolute strength of the organisation. Prahalad and Hamel (1990) narrow the parameters for core competency by defining it as the underlying skills, technologies and organisational capacities that can be combined in different ways to create the next generation of products and services. Under this definition, a core competency is tied back to the strategic and functional capabilities of Day's (1994) resource analysis. However, Day's approach looked at the current capacity and ability, whereas the Prahalad and Hamel definition is a more proactive statement of innovation.

On the basis of the proactive nature of Prahalad and Hamel's definition, three tests are used to identify potential competencies:

- Does the competency provide potential access to a wide variety of markets? Core competency assumes a non-niche strategic orientation. For the purpose of the analysis, a competency can be identified by the ability to access a wide variety of markets or provide a wider set of product solutions for customer needs.
- Does the competency have the capacity to make a significant contribution to the core value proposition received by the customer? A competency needs to add to the value received by the customer to be beneficial in producing a competitive advantage. This is where an understanding of the customer as stakeholder can be used to assess or support claims for core competencies.

- Is the competency difficult for the competitor to copy? Unique core competencies that give value to the customer provide a greater competitive advantage than easily replicated alternatives.

The role of the core competency analysis is to focus on the strengths of the organisation, and the best fit between the organisational strength and the needs of the marketplace. However, identifying a core competency in an organisation is prone to difficulties and certain vulnerabilities. Snyder and Ebeling (1992) caution against identifying activities and attributes such as marketing strength or product quality as competencies. Similarly, core competencies, by their nature, will be limited in number and should underpin all strategic decision making. If not, then what has been identified may not be a competency, but an organisational process or attribute.

Analysis V: Porter's Value Chain

The value chain concept is based on Caves and Porter (1977) and Porter's (1985) conceptual model of the organisation as a holistic entity where each value-adding component activity is linked to the final value offering by the firm. As such, all activity in the organisation could be seen to contribute to the aggregate of the value offered to the consumer. Porter's Value Chain can be used as a system for determining the presence of a competitive advantage *and* as an exploratory tool to determine if competitive advantages can be generated by linking component parts of the process. For example, whilst the initial analysis may demonstrate an organisational strength in knowledge management regarding the seasonal demand for products from the customer and competitive efficiencies in accounts financing, the merger of these two factors can create a competitive advantage as simple as creating a custom payment schedule that works in tune with the customer's cash-flow situation.

In examining the value chain, Porter's model splits the activities of the organisation into primary value creation—the direct contributors to the final value offering made by the organisation—and the secondary components that are support acitivites to the primary value creation (Hooley, Saunders & Piercy 2004; Viljoen & Dann 2003; Porter 1985).

Components of primary value creation include:

- *inbound logistics*—the process of managing the input flow of resources into the company. This includes controlling physical products, financial input and human resources, and the use of just-in-time manufacturing relationships with suppliers to maximise value and minimise resources being warehoused. Changes to the value chain in inbound logistics has the most direct impact on the supplier stakeholder group, and is most influenced by the relationship the organisation has with its suppliers.
- *operations*—the process of turning the input into saleable value offerings for the customer. Traditionally, the operations phase has been seen as the largest area for value creation and value addition as it creates the products designed to meet the needs of the consumer. Adjusting the operations level will involve employee and

management stakeholder groups, as well as the necessity to ensure that the needs of the consumer are being met, both in their capacity as customers and as stakeholders.

- *outbound logistics*—the delivering aspect of the 2004 definition of marketing, which represents the assembly, processing, storing and shipping of the product to the consumer or the distribution channels. This involves the opportunity for the organisation to engage in just-in-time production, and to develop and enhance relationships with its distributor stakeholders to create value.
- *sales*—representing the communication of the value offer to the customer, and the value exchange process. The sales aspect of the value chain can also incorporate any aspect of marketing which adds value to the product offering, such as branding, image or reputation. Obviously, this represents the consumption stakeholder context, and changes to this stage of the process will impact directly on the consumer stakeholders. However, it is also possible that distributors (such as retailers and on-sellers) may need to be considered active stakeholders in the sales/consumption process.
- *service*—the after-sales augmentation of the physical product's value offering or the delivery of the service product's value. This area includes any effort undertaken to improve the level of value the consumer receives from the product offering either through training, after-sales support, repairs, installation or product returns. This involves both the consumer and employee stakeholder groups. Changes to the service aspect of the value chain may also involve the broader environment stakeholder context as the organisation educates the population as to the importance of their product's value, thus increasing its desirability and value to the consumer. Influencing attitudes towards a product can invoke conflict with community and social lobby group stakeholders.

The second part of the Porter Value Chain involves the support activities. This covers those activities required to maintain the operation of the organisation, but which do not directly contribute to the value offering made to the customer. These include:

- *procurement*—the process of acquiring the resources needed for each of the value adding components of the value chain. This incorporates the interface between the employee and supplier stakeholders, and the business-to-business relationship between the organisation and suppliers. Procurement interacts with the value chain element of inbound logistics. It also encompasses the role of the organisation as a consumer as it represents the acquisition of supplies for the firm.
- *technology development*—the process of ensuring that the technology used by the value addition processes has the best possible fit with the organisation, and that the most appropriate (not necessarily the newest) technology is available to the firm.
- *human resources*—the capacity of the organisation to ensure that the right sets of people, skills, abilities and motivation are available to the organisation as employees, contractors or other participants in the production process. This area intersects with the stakeholder interests of the unions, employees, and management.

- *systems*—the efficient and effective operation of the organisation through the management and control of organisational processes, systems and procedures. The role of the systems element of the value chain is to ensure that the value addition components (e.g. services, sales) can interact and communicate as effectively as possible. This leads to micro-stakeholder issues between subsets of the organisation's employee stakeholders (e.g. the subdivisions of sales and logistics, or production and inbound logistics).
- *marketing*—the organisation's coordinated efforts to define 'value' in terms of how the customer perceives it, and to create a value offering that meets the customer's needs and wants. The contemporary definition of marketing involves all stakeholder groups with an emphasis on the consumer as both stakeholder and customer.

Analysis VI: employees

The final aspect of the internal analysis of the firm is to take stock of the organisation's human resources as part of the marketing capabilities of the firm. This involves the examination of three areas:

- employee satisfaction
- employee involvement in the value process
- employees in the marketing process.

The employee stakeholders are a critical part of the business process as they are usually responsible for the development of the product, implementation of the strategy, and interaction with the customer. Consequently, failure to examine the strengths and weaknesses of the organisation's employee group can limit the effectiveness of the implementation of any marketing strategy. In addition, assessments of the human resource strengths of the organisation can be used as part of the business competitive position analysis for the Directional Policy Matrix models.

The value of employee satisfaction

Employee satisfaction is an integral part of successful relationship marketing as summarised in the findings of Brooks (2000) on the dynamic between customer satisfaction and employee satisfaction. These findings include:

- One of the strongest predictors of employee satisfaction is the level of internal service support available to the staff who interact with the customer. These are the areas covered by the systems and procurement elements of the Porter Value Chain model.
- Employee retention rates are related to customer retention rates in that higher employee retention indicates high customer retention. This was addressed in the research literature as being indicative of the level to which the organisation pays attention to its key stakeholder groups.
- Between 40 and 80% of customer satisfaction can be attributed to employee satisfaction.

Benchmarking employee satisfaction can also be seen as a proxy measure for customer satisfaction insofar as rapid shifts in the levels of employee satisfaction will likely be reflected in the customer base.

Benchmarking employee involvement

Measuring employee satisfaction can be done through three methods. First, it can be handed off entirely to the human resources department as part of their organisational responsibility, and only queried by marketing during times of planning and analysis. Second, employee satisfaction can be directly measured as internal market research, although this may lead to demarcation disputes with the HR department. Finally, Kaplan and Norton (1996) examine measures of suggestions made and implemented. This includes implementing knowledge management and tracking systems so that employee feedback can be lodged and, when it is implemented (or rejected) by the organisation, attributed back to the original employee who made the suggestion.

Benchmarking employee satisfaction

Employee satisfaction benchmarking is required as part of an internal audit of the state of the organisation prior to embarking on a strategic marketing planning process or implementation and is less complex than those required by human resources. Kaplan and Norton (1996) regarded the main elements of an employee satisfaction benchmark for the balanced scorecard as being:

- overall satisfaction with the company and the direction of the organisation, which is a composite measure of the interaction between the organisation and the employee stakeholder group
- recognition for job performance, including rewards for high performance and disincentives for under performance
- involvement with the decisions and decision-making process, which would assess areas such as involvement as organisational stakeholders and the interaction between management and employees
- access to information and resources to perform the job required to the standards required, which is a measure of the effectiveness of Porter's systems and procurement elements of the value chain. This also includes support from the internal processes of the organisation including management and human resources
- active encouragement to be creative and to use initiative.

Balanced scorecard element 4: organisational innovation

The fourth and final aspect of the balanced scorecard method is based on organisational innovation. Kaplan and Norton (1996) integrated employee satisfaction as part of their

original model of the balanced scorecard. However, for the purpose of this book the ability of the organisation to develop through innovation and organisational knowledge management is considered as a separate category, although aspects of this will interact with elements of employee satisfaction, and involve the employee stakeholders group.

Defining organisational innovation

Organisational innovation relates to the ability of the organisation to develop new processes and ideas, or to build upon existing processes to increase efficiency, effectiveness or organisational output. It is not directly related to the new product development process although an organisation with a strong emphasis on new product development will have a higher level of innovation in its organisational culture. That said, an organisation with an emphasis on product refinement will place greater emphasis on the evolution and development of improved processes rather than new processes.

Benchmarks of organisational innovation

One difficulty to expect when conducting an internal analysis aimed at determining nebulous concepts such as 'organisational willingness to embrace new concepts and processes' is the blurred line between employees and organisational culture, since the organisational culture consists of management and employee attitudes. Characteristic traits of organisational innovation include:

- availability and use of internal skills development and reskilling programs. For example, where technology changes have improved operating conditions or introduced new techniques, organisations which are orientated towards innovation and change are more likely to set aside resources to reskill or upskill their employees.
- evidence of continuous quality improvement measures, such as published benchmarks for throughput, days without accident, satisfied customer levels or other indicative quantitative figures that are displayed.
- internal organisational competitiveness based around benchmarks and quotas. For example, where an organisation rewards the success of particular business units in achieving goals, it increases the likelihood of those units accepting new methods and techniques that could enhance performance to meet (and exceed) those targets.

From a marketing analysis perspective, the main reason for assessing the level of internal innovation is to assist in preparing the internal marketing plan, which will be used to explain the outcomes of the strategic planning process to the employee and management stakeholder groups.

Conclusion

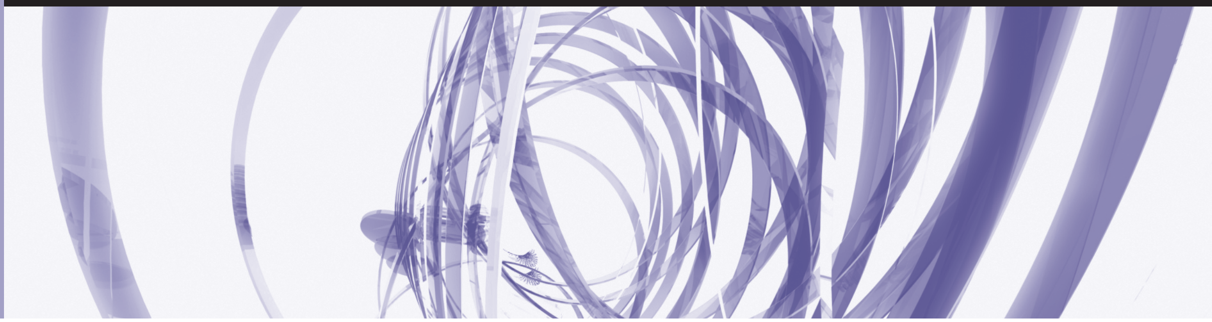
Quality marketing strategies can only be developed after a thorough analysis of the organisation and its ability to meet opportunities in the marketplace has been undertaken. In this chapter, the focus is on internal analysis. There are many frameworks which can be used to conduct an internal analysis, however for the purpose of this text the broad framework of the balanced scorecard has been used. Traditionally the health of an organisation has been measured predominantly in financial terms such as profit, share price or return on investment. The danger with focusing too heavily on financial measures is that short-term financial gains can often lead to a weakening of the organisation and ultimately to longer-term losses. The balanced scorecard method broadens the focus of measuring success to include customer relationships, internal business issues and innovation, in addition to finance.

Marketing strategy derives from the organisation's broader corporate strategy however the internal analysis here is more focused on consumers and stakeholders than is usually the case with a similar analysis undertaken at the whole of organisation level. In particular the chapter gives an overview of the importance of treating the consumer as a stakeholder by focusing on issues such as relationship building, satisfaction and loyalty as well as the costs of acquisition and retention. In addition, the increasing marketing focus on providing marketing metrics and satisfying shareholder value is addressed.

As well as knowing the broad concepts of what should be measured, it is important to have an idea of how these concepts are measured. Consequently the chapter also reviews some basic formulae for determining the value proposition and shareholder value. Undertaking a comprehensive internal analysis of the capabilities of the organisation to respond to different opportunities in the environment, allows the marketing strategist to focus only on those opportunities which are potentially profitable to the firm, and to develop realistic and effective marketing strategies.

Analysis 2—External analysis

CHAPTER 5



Introduction

Chapter 5 examines the process of conducting an external analysis of the organisation with a specific focus on how the firm is positioned relative to the competition, and the type of competitive environment the firm operates in. Techniques for evaluating market attractiveness are also discussed. Finally, an overview of the regulatory restrictions and legal framework within which Australian marketers operate will be given.

Undertaking the external analysis

As mentioned in Chapter 4, there is considerable debate as to whether the external analysis should be conducted before or after the internal analysis. In this book, external follows internal analysis. There are five areas of external analysis that need to be considered by the organisation:

- industry analysis
- market attractiveness analysis
- customer analysis
- competition analysis
- business environment analysis.

One of the benefits and features of the external analysis is the interconnectivity of the process where information from one analysis (e.g. market attractiveness analysis) can inform other aspects of the process (customer analysis) and vice versa. Whilst these elements are presented as separate functions to ensure that each aspect is covered in this chapter, each element (e.g. industry, market and customer) is interconnected in the business world. Although the customer also featured as an aspect of the internal analysis, the external analysis looks at the current and potential needs, wants and characteristics of the potential customer base as an external factor in the operation of the firm. The external customer analysis is a critical component in understanding what product or value offering needs to be presented to the market to acquire new customers.

Industry analysis

Industry analysis has three purposes in competitive marketing strategy. First, it identifies the attractiveness of an industry for an organisation and its financial backers. This information can then be used to develop the Directional Policy Matrix models from Chapter 2. Second, industry analysis is useful for identifying the current cycle the industry is facing, and the market conditions that arise from that point in the cycle. Finally, the analysis assesses the extent to which each element of Porter's (1980) Five Forces Model is present in the market, and whether additional forces need to be considered.

Industry attractiveness

The use of Composite Portfolio Models such as the GE/McKinsey Directional Policy Matrix Variant require organisations to assess themselves on the two factors of industry attractiveness and the business's competitive position. Business competitive position was covered in the previous chapter (Chapter 4, Internal analysis). Industry attractiveness is a complex variable based on the available resources within the market, such as supplies, raw materials, available employees with requisite skills, and avenues for distribution. In many respects, industry attractiveness analysis is the extent to which the industry can meet the organisation's internal needs and wants for skills, supplies and services. Consequently, the needs of the industry stakeholders such as suppliers, distributors, financiers and creditors need to be considered in any analysis.

Viljoen and Dann (2003) outline a series of factors that determine the attractiveness of an industry to an organisation. These include:

- *suppliers*—including the range of suppliers, their relative pricing power based on the level of competition amongst suppliers, quality of their products, flexibility and ability to deliver custom products, willingness to engage in just-in-time delivery. In addition, the suppliers' market with the consumer is important. For example, Intel has invested heavily in developing a positive reputation as a component part in end-user products, a reputation which has positive benefits at both the business-to-business and consumer level.

- *human resources*—which examines the availability of the requisite level of skilled employees within both the broad labour market and the specific regional areas of interest to the organisation. Shortages of skilled labour can impact on the viability of an organisation, increasing production costs and the relative power of the employee stakeholders.
- *physical resources*—covers the availability of the requisite materials for the creation of the product or service. This includes office and warehouse space, retail shop frontage or any other physical resource. In addition, if the organisation requires specific physical resources, such as access to water for irrigation, or access to train lines for shipping, these issues are part of the physical resource analysis.
- *size and growth*—refers to the broader performance of the industry over a wide range of markets, and includes factors such as the rate of growth and the number of competitors that can be supported by the industry. This element can also be used in conjunction with the BCG Growth Share Matrix.
- *distribution channels*—which is an analysis of the potential distribution outlets for the product including internet delivery, delivery direct to customers, extended distribution chains, wholesaler and retailer outlets. In addition, it includes an assessment of the extent to which a single organisation can dominate a distribution channel to create a monopoly or significant barrier for others accessing the market.
- *costs*—which relate to the influence of financial price on the success of the industry's product offerings. Competition in many cases is based on a complex intermingling of perceived quality, service provision and unique product characteristics. However for some products and customers price is the dominant factor in the purchase decision and therefore the company's success. The cost element of the analysis includes the review of what aspects of the external market can be used for cost leadership strategies, e.g. can cheaper distribution be acquired? Are there savings that could be produced from different supplier agreements?
- *trends*—which are the examination of the nature of the industry and any significant changes that are occurring or have potential to occur in the near future. Near future in this context is considered to be a series of staggered time periods from six months to eighteen months to three-, five- and ten-year periods. Trend spotting is the subject of significantly large numbers of books by 'futurists' who attempt to predict the future development of industry trends.
- *key success factors*—which are the small number of consistent factors that assist the success of organisations within an industry, and whilst this is similar to the core competency concept, it is externally driven as it is based on the success of other organisations in the industry. For example, if the industry is driven by low-cost products and low mark-ups, a key success factor is the ability to restrict production costs.

- *structure*—which determines the competitive characteristics of an industry. It is based in part on Porter's Five Forces Model, which is examined in detail later in the chapter, and includes new entrants to the market, the suppliers, consumers, what product substitutes are present, and the range of competitors in the marketplace.

The attractiveness of an industry is based in part on how well the industry can meet the needs of the organisation as the organisation attempts to meet the needs of its customers. A weak industry with limited capacity to service the needs of the organisation is as great an impediment to success as weak demand for the product offering.

Industry life cycle

The second part of the industry analysis is the examination of the state of the industry in terms of where it is along a continuum from emergent industry to those in late stages of decline (Proctor 2000). Porter (1980) originally defined the industry life cycle as consisting of three stages—emergence, maturity and decline. Whilst resembling a truncated product life cycle, the industry life cycle can be expanded to introduce shades of grey into the black and white birth/peak/decline model. For example, Proctor (2000) and Hooley, Saunders and Piercy (2004) both include the additional stage of 'transition to maturity'. Proctor also adds the post-decline phase of 'hostile' market. For the purpose of this book, industry life cycle categories are defined as:

- *emerging/developing industries*—which are those industries that have recently developed around a new product, new idea or new market segment. These markets can emerge from existing markets in decline due to the market being revived through innovation, or may result from a new market segment emerging. Analysis in new industries should be orientated towards primary research, marketing research and the development of effective mechanisms for capturing marketing intelligence as it occurs. Due to the new nature of the market, there will be less opportunity to work with established assumptions regarding the consumer's needs and wants.
- *transitioning to maturity*—which are those markets that are in the growth process, but which have yet to peak to maturity. These markets are characterised by slowing rates of growth when compared to the emergent markets, and increased levels of competition. Analysis for the transition period can include the use of marketing intelligence acquired during the emergence phase, and through competitor analysis.
- *maturity*—which is characterised by the relative stability of the market as indicated by the cessation of growth, excess capacity in the market and increased price pressure emerging from competition and consumer power. In addition, the decline in growth coupled with excess production capacity usually results in a much broader range of products from the organisation and its competitors. Differences between competitor offerings are marginal and a heavy

emphasis is placed on the intangible assets of the firm to differentiate products in the marketplace. Analysis at this stage is focused primarily on competitors, as growth in a mature market requires the organisation to take a customer from its competitor (and vice versa).

- *transition to decline*—which is the phase after maturity has been reached, and when the industry finds sales decreasing and the size of the market contracting. It is also characterised by the first wave of competitor withdrawals from the marketplace as profits are cut away by price competition and the need to dispose of the excess capacity. Analysis for this phase should begin to reintroduce primary data collection to assess the broader state of the industry to see if the decline has been caused by product substitution, lack of demand, or other factors. Observation of competitors continues in order to assess their movement into withdrawal, or if they are showing overt signs of attempting to revitalise the market. This transition is not always inevitable with some products able to be successfully re-positioned to extend the maturity phase of the product life cycle.
- *decline*—which is the point in an industry where the market segment has either ceased to be viable, or the need is being served by a different technology or value offering. For example, although the market need for musical entertainment has been consistently strong, the industries providing music such as piano rolls, live orchestras, 78 rpm vinyl albums, cassettes and mp3 players have been through different industry phases. Marketing during the decline phase is covered further in Chapter 13. The priority in the industry analysis stage is to determine if the decline is permanent, or if there is an opportunity to revitalise the market.

The value of the industry cycle as an analytical tool is to determine the point which the industry is presently at, as this will influence how the organisation can and should react in terms of setting strategies and objectives. Different industry cycles will also influence the success of different strategies based on prevailing industry conditions. However, at this stage of analysis as a part of marketing strategy development, it is enough to be able to place the industry in a position along the emergence–maturity–decline curve so this knowledge can be used for strategy and objective setting.

Five Forces analysis

The third part of the industry analysis is to assess the structure of the overall industry using Porter's Five Forces as a guideline. In brief review, the Five Forces can be summarised as:

- competitors and the rivalry amongst competitors
- new entrants, which is the threat of new competitors plus the barriers to entry facing a new competitor
- substitutes, which is where a market need can be met by an alternative product
- bargaining power of the suppliers
- bargaining power of the buyers/customers, which is a reflection of the strength of the consumer.

The Five Forces Model is also similar to the Viljoen and Dann (2003) factor of 'structure', which was based on the concept. In terms of the external analysis process, the value of the Five Force Model is to use it as a checklist for assessing the structure of the industry. Table 5.1 presents the Five Forces as a series of questions to be answered by an analysis.

TABLE 5.1 Five Forces checklist

- How competitive is the marketplace?
- What competitive conditions is the firm is facing? For example, is there potential for market growth? Does growth come from expanding the market or by taking market share from competitors?
- Are products mostly undifferentiated or are there opportunities for specialist products?
- Is this a closed or open marketplace?
- What is the realistic likelihood of new competitors entering the market?
- What entry barriers exist, and can those barriers be influenced by the firm's activities?
- What sort of substitute products can the customer use to meet the need that the firm's product is currently meeting?
- Who holds the power in the relationship between the firm and the suppliers?
- Who holds the power in the relationship between the customer and the firm?

As mentioned in Chapter 2, the Five Forces are not necessarily the only major factors influencing the structure of the market. Additional areas such as regulation and the involvement of governments should be added to the analysis.

Market attractiveness analysis

Market attractiveness is the combination of the financial viability of a market, the size of the existing and potential demand for the organisation's value offering, the overall size of the market, and what opportunities for growth exist in the marketplace.

Having assessed the state of the industry, the second level of external analysis is to determine the attractiveness of the market in terms of the following four elements:

- market definition
- market potential
- market demand
- market growth opportunities.

Market definition

Market definition is how the organisation describes its current and potential customers based on their needs and wants which are being met or which could be met by a value offering from the organisation. A narrow market definition based on a product offering

(e.g. cola) will not necessarily accurately reflect the market based on the need being filled by the product (e.g. thirst). In addition, with the new emphasis in marketing on 'creating, communicating and delivering value' instead of 'ideas, goods or services', markets need to be defined around value rather than product portfolios. Analysis of market definition is based on defining the value offering of the organisation (Chapter 4), market segmentation (Chapter 6) and customer analysis (examined later in this chapter).

Market potential

Market potential is the maximum number of customers who can, and will, enter a specifically defined market. Assessing market potential is a question of examining the approximate size of the market by measuring the target population in terms of the total number of current customers and potential customers. Where the current customer base is approaching the total number, the market has limited potential for expansion and growth, and vice versa. Where the number of potential customers in a market is smaller than the total number of current customers, market share has to be gained at the expense of competitors.

Measurements of market potential are based on the number of customers in a market, rather than volumes of units sold. These measurements can be acquired through direct market research, secondary research and observation of competitor sales figures listed in annual reports and other public documents.

Market potential can also be examined in terms of the inhibitors that are influencing the market's capacity and willingness to adopt the value offering. These inhibitors include:

- *awareness of the benefits of the value offering*. This requires the market to be aware of the product or service offering, what it does to meet the customer's needs, and what value it offers ahead of competing alternatives.
- *availability of the value offering*. Although the definition of marketing states 'creation, communication and delivery', some markets may not be able to access the value offering due to lack of distribution channels. Availability is also influenced by the amount of secondary support and secondary products that are available for use with the primary value offering. For example, although the Nintendo DS handheld game system is widely available, there are a limited number of games for the system. Consequently, the value offering (portable entertainment) is not being made available due to the lack of secondary products (games).
- *ability to use the value offering*. This consists of the consumer possessing the requisite skills, intelligence, education or abilities to make use of the value offer (e.g. computer, online subscription), and the existence of appropriate secondary systems (e.g. electricity, internet access).
- *the product suffers from benefit deficiency*. Benefit deficiency is where the product's core value does not meet the needs of the consumer, even though it may be meeting the needs of other consumers in the market. For example, many Microsoft customers have not upgraded their Microsoft Office software because the subsequent releases had insufficient benefits, or offered insufficient value, compared to their current solution.

- *the product is not affordable*. Affordability combines the financial costs of the value offer with the non-financial elements such as time, prestige or effort. Although the value offer would satisfy the needs of the customer, they may not be able to afford the financial price (e.g. expensive gym membership fees), or they may not be able to forgo the other opportunities (e.g. time spent in gym is time not spent on other activities), or the ancillary costs may price the core value offering out of reach (costs of clothing and shoes for training at the gym).

Understanding the inhibitors to maximising the market potential requires an understanding of the consumer needs and wants through the use of the customer analysis in this chapter.

Market demand

Market demand is a relatively straightforward concept of totalling the aggregate demand of new purchasers (new customers) and new purchases (existing customers). As with any mathematical model, complexity arises when the demand is calculated over time, as each new customer becomes an existing customer who will repurchase the value offering again at a later point. Market demand is influenced by the market potential, since first time purchasers will eventually decline over time as the current customer base reaches the market potential. As a consequence, market demand is also tied into the product life cycle concept (Chapter 2), as peaks and troughs in demand for the product occur as new customer numbers plateau, and the organisation relies on repurchase by existing consumers.

Market growth opportunities

Market growth opportunities are those readily identifiable aspects of the market that can be used to form the basis for setting objectives and planning strategies. This part of the analysis process is based on drawing conclusions from the previous elements. For example, a market with poor potential based on benefit deficiency to the value offering could be identified as a target for growth based on new products or revision to existing products.

Customer analysis

Customer analysis is the external process of examining what value offering is being sought by individuals or groups within a market identified by the market analysis. Whilst markets are conglomerations of consumers, the customer is the person who is responsible for selecting the value offering and, consequently, is the person the organisation must address rather than a generic 'market'. As a result, the questions of market profitability are addressed in the customer analysis as measures of the profitability and sustainability of a market segment of customers.

Customer analysis is also where the issues of the value offering of the customer are examined, along with the stakeholder issues of the customers and the consumption context. It also draws heavily on consumer behaviour theory and the practical aspects of market

research and, as with the rest of the book, there is an assumption of prior knowledge of consumer behaviour theory, and marketing research theory and practice.

Identifying the customer

The first step is to identify the customer, and whether the analysis will be dealing with business-to-consumer or business-to-business customers. It is possible for an organisation to have both business-to-business and business-to-consumer relationships to manage as a result of distributing through retailers and distributing directly to the end consumer.

Business-to-consumer decision process

The business-to-consumer decision-making process is based on the Engel, Blackwell and Miniard (1986) five-stage model. The components of the model are as follows:

1. *Problem*. This is the first stage where the consumer recognises that they have a need, want or have run out of the product that was previously used to satisfy their needs.
2. *Information search*. The second stage is where the consumer conducts an information search to find alternatives to solve their need.
3. *Evaluation*. The evaluation phase is where the consumer assesses the value offerings against their needs to identify which product/service has the most chance of satisfying those needs.
4. *Purchase decisions*. This phase incorporates store selection, the final purchase decision and the actual purchase behaviour.
5. *Post-purchase*. This is where the product is used, and any secondary products are consumed in the use of the primary product (e.g. toner cartridges for a colour printer).

The importance of the decision-making process is to understand how the organisation interacts with the consumer in each of these stages, and identify where the organisation has strengths or weaknesses. This analysis is critical when addressing different strategies for growth or value addition. For example, really new product offerings require the customer to realise that they have a need (problem stage) and that this previously unrealised need can be solved with the organisation's really new product (information search, evaluation). In contrast, a growth strategy based in a crowded market will require the consumer to select the organisation's product ahead of the competitor options. In this example, the emphasis is on the evaluation and purchase decision stages. Finally, if the organisation is attempting to increase the volume of products purchased by existing consumers, the post-purchase element of the process is critical to determine levels of satisfaction, and whether the value offering is meeting the customer's needs.

Business-to-business decision process

If the end consumer of the product is another organisation, the business-to-business purchase decision process should be used as the basis of the analysis. Robinson, Faris and Wind (1967) outlines an eight-step model of the business decisions process:

1. *Problem recognition*—in the business sector this may involve out-of-stock errors, or the need to find a supplier of parts and materials for a new product.

2. *General need description*—this stage outlines the company's broad set of needs for the product and is followed by a narrower set of product specifications.
3. *Product specifications*—unlike consumer purchasers, business purchasers tend to have exacting standards for their needs and wants, and this stage is where those standards are set.
4. *Supplier search*—this can occur proactively as the organisation seeks potential clients, or reactively as it puts out calls for tenders.
5. *Proposal solicitation*—this is where multiple suppliers are selected, either by open tender or by approaching the potential candidates for quotes.
6. *Supplier selection*—this is the business equivalent of the purchase decision phase where suppliers are chosen and products are purchased.
7. *Order-routine specification*—the order-routine specification includes the establishment of the business relationship, reordering procedures and other elements such as just-in-time manufacturing and delivery.
8. *Performance review*—the final step in the process is the ongoing review of the business-to-business relationship.

As with the consumer decision process, the value of this model in the analysis stage is to ascertain where the organisation has strengths and weaknesses in relation to its involvement in the business buying decision process. For example, organisations with a focus on developing new business-to-business products will need to have strengths in creating problem recognition, proposal solicitation and supplier selection. Simply being adept at creating demand will not assist the organisation if they cannot make it through the proposal and supplier selection process.

Market segmentation

Having set the broadest level of market segmentation (business or consumer), the next part of the analysis is to review any market segmentation strategies, and the potential market profitability of those segments currently not being serviced by the organisation. Current customer needs and wants were addressed in the internal analysis (Chapter 4). For the external analysis, market segmentation is a review of the potential market, based partly on the market attractiveness analysis above, but reviewed through a narrower set of parameters to identify potential new segments.

Parameters for a market segment

Kotler (1998) puts forward the basic 'who, what, where, when, why and how?' approach to market segmentation with a methodical checklist for knowing the customer:

- Who constitutes the market segment?
- What does the market segment buy/want in the marketing relationship?
- Why does the market segment buy/want the marketing relationship?
- Who participates in the buying/marketing relationship process?
- How does the market segment buy/participate in the marketing relationship?

- When does the market segment buy/want to be part of the marketing relationship?
- Where does the market segment buy/want to be part of the marketing relationship?

Addressing the questions raised in this aspect of the analysis requires the organisation to revisit its knowledge of consumer behaviour (or business-to-business marketing), and to engage in market research techniques such as perceptual mapping to understand the consumer. One of the truisms of marketing strategy appears to be that the shorter the section is in a text such as this, the longer the process will be for the organisation in practice. In this case, engaging in market segmentation and customer analysis is a significant and large process that will provide much of the information required for strategy setting and the development of the marketing plan.

Market segmentation analysis

As part of the segmentation process, the market segments have to have their own requirements to be a useful contribution to the external analysis process. Market segments have a series of requirements, which include the need to be unique, measurable, accessible, responsive and substantial. Uniqueness is the reason to create the new market segment and not use an existing one or a non-segmented strategy. It requires the segment to have a distinct (and preferably measurable) set of characteristics, responses to marketing tactics and value offerings. Measurability means that the segment must be based on a definable series of characteristics that can be used to recognise it. A market defined as 'school students' is less measurable than a market such as '13–16 year male and female high school students in geographic region of the Eastern seaboard with access to broadband internet at home who have an interest in music downloading'. Measurability also assists in determining the accessibility of the segment to the organisation through distribution chains, electronic sales or other methods of reaching the customer and providing the value offering to them. Barriers to accessibility also include geography (inland versus coastal deliveries of fresh fish), social expectations (is the product 'appropriate' by the social norms of the target market?) or language and literacy (does the customer have sufficient language skills to use or acquire the product?). Responsiveness to marketing strategy and tactics determines whether the segment will be a worthwhile market for developing a separate marketing communication. If this new segment will react in a similar manner to related market segments, then either the communications strategies need to be further refined, or the segments can be merged to create an economy of scale for the communications. Finally, the segment needs to be substantial or sustainable in size, profitability, potential growth or any other appropriate financial measure. There are limited reasons for addressing unsustainable markets, and unless the organisation has a specific mission or objective that requires it to service an unviable market as part of a broader community obligation, these should not be part of a segmentation strategy.

Segmentation is addressed again in Chapter 6 as part of the objective setting, and plays a significant role in the use of niche strategies (Chapter 12). In general, the role of

segmentation in the external analysis is to classify potential target markets in terms of unique characteristics, financial viability and overall desirability to the organisation.

Consumer behaviour revisited

As mentioned previously, customer analysis dealing with the individual, rather than the organisation, depends heavily on consumer behaviour theory. Innovation adoption and Belk's (1975) simplified model of consumer behaviour were first mentioned in Chapter 1. As well as these two models, an additional consumer behaviour model is included in the analysis: the role of the customer.

Innovation adoption and external analysis

Innovation adoption and the different types of innovation are an integral element of any new product strategy, and consequently the customer analysis needs to include an assessment of the customer's involvement with the product offering. This analysis can involve a variety of methods, from using the product life cycle (Chapter 1), through to an investigation of the organisational history, and the release dates for products in the market segments. The major consideration in undertaking an innovation assessment is to remember that the innovativeness of a product is determined by the market's exposure to the product, or similar products. Consequently, it is possible for an organisation to have old products (from an organisational sense) be considered innovations, or to have new products (products the organisation has not previously offered) which are continuous innovations in the marketplace.

Belk's simplified model of consumer behaviour

Like the decision process models above, the value of the Belk model is in its use as a framework for analysis. The Belk model's four elements of situation, product, person and behaviour can be used in the external analysis as follows:

- *Situation*—understanding the purchase situation including the external influences on the decision process, such as pressures on the purchase decision from societal influences, consumer role expectations, and the substitute products available from the competitors.
- *Product*—although the organisation's value offering is covered in internal analysis elements such as the value chain, this also incorporates the external analysis components of competitive advantage (covered later in the chapter).
- *Person*—understanding the consumer's internal mental processes, knowledge, memories, skills and abilities is the core of the customer analysis, and incorporates a wide range of consumer behaviour models.
- *Behaviour*—the final element is to understand how the person, situation and product led to the observable outcome of purchase, trial, continued information search or rejection. Understanding how the organisation's value offering is used in trial adoption or actual adoption, or how it was used and rejected assists in determining the actual value offering as perceived by the firm.

Roles of the customer

In addition to the innovativeness of the product, and the consumption situation, the third area of interest for customer analysis is to review the role played by the consumer in the purchase process. The five roles are also interrelated with the five stages of Engel, Blackwell and Miniard's (1986) model, and the eight stages of Robinson, Faris and Wind's (1967) business decision process. Table 5.2 summarises the interaction of the consumer roles with the organisation and individual consumption decision models.

TABLE 5.2 Comparison of the consumer roles

Roles	Individual decision	Business decision
Initiator	Problem	Problem recognition General need description Product specifications
Influencer	Information search	Supplier search Proposal solicitation
Decider	Evaluation	Supplier selection
Purchaser	Purchase decision	Order-routine specification
User	Post-purchase	Performance review

Table 5.2 is based on the assumption that the five roles can be either played by the individual consumer, or that there are external influencers in up to four of the five roles—assuming that the decider or purchaser is always on the receiving end of the role influences. The five roles are:

- *initiator*—the person who notices the need or want in the first instance.
- *influencer*—the consumer or consumers who have the most sway over the attitudes of the decision maker, and who exert the most influence. For example, a consumer with no interest in high technology will turn to a more interested friend for advice. That friend, with their greater enthusiasm, will act as a direct influencer on the consumer's purchase.
- *decider*—the person ultimately responsible for making the purchase, trial or rejection decision.
- *purchaser*—the person who pays for the value offering. In the case of proxy purchasing by parents for children, the purchaser may not actually be the influencer, decider or user, but still has to pay the bills.
- *user*—the person to ultimately receive the value offering and make use of it to solve their needs and wants.

The value of this process in the analysis is to determine which market segments occupy which roles, and to adjust marketing strategies to those roles and segments. For example, whilst the child is the end user of most toys, books and education products, parents act in the gatekeeper role of being purchasers. Consequently, targeting the market for the child also requires a consideration of the parental market segment to determine barriers to purchase (e.g. cost, moral objections to video games, preferences for suitable reading material).

Analysis methods and market research in consumer analysis

There are three main areas of market research data that can used in consumer analysis: internal records, existing information or the production of a new, customised study. There are two specific types of analysis to be considered in the external analysis of the consumer. These are:

- *lead user analysis* which examines how the customer creates their own value from the value offering of the firm
- *the Kano Method* which is a technique for identifying the sources of customer satisfaction and value.

Lead user analysis

Lead user analysis was developed as a response to the inherent creativity of the consumer, and the market opportunities that are developed from engaging the consumer as a part-time designer for the firm. Use innovations, where the customer uses the products in a way not originally considered by the firm, can sometimes lead to profitable market niches. For example, if the customer is using the product for a purpose that was not originally considered by the organisation (e.g. packaging material as insulation), they may have uncovered a profitable secondary market for solving an unforecast market need (e.g. temporary housing repairs).

The process of lead user analysis is a four-step routine outlined by Best (2005):

- *Step 1*: Identify lead users who have extended the use of the product.
- *Step 2*: Study how lead users have extended the product usage. Some extensions may be the basis of meeting the needs of an unrecognised market.
- *Step 3*: Discover how products could be modified to improve usage. Use innovation may include customisations to the product to compensate for mis-features (e.g. loose parts, uncomfortable handgrips) or may be more complicated (case modifications to allow for larger batteries).
- *Step 4*: Develop a more complete customer solution or new product. Commercialisation of the revised product still needs to be treated as a new product development process to ensure it can deliver a product of value to the organisation and market, even where the revised product is based on the behaviours of consumers in a current market.

Use innovation occasionally causes problems for the organisation where the product being used was sold below cost as part of a wider strategy to gain market share, then recoup costs on secondary products. Where this occurs, the organisation will sometimes see its lead user consumers as competitors and threats, and respond with lawyers and hostility. This is a poor marketing strategy, given that a use innovation is created by lead users, and those lead users are sufficiently motivated by the product to expend their time, effort and resources to create something new. It is usually a much more sensible strategic decision to review the actual losses from the use innovation. If these are widespread, then this can be indicative of a failure of the below-cost strategy, and should encourage the organisation to set a more realistic pricing strategy. Attacking the user for having a creative use for a product they have purchased from the organisation is usually grounds for bad publicity, as well as poor business practice.

The Kano Method

The Kano Method is a complicated process of producing a prioritised list of features for the value offering to the customer. The Kano Method is explored further by texts detailed in the annotated bibliography. In summary, the Kano Method can identify what the consumer does, and doesn't, want in a product offering by matching the actual product feature with one of five idealised types. The five product feature types of Kano et al (1984) model are:

- *'must be' features*—which are those features that have to be present in the value offering, but which are simply assumed to be present by the consumer and are rarely mentioned. If the value offering does not contain the 'must be' feature, then it will not be considered by the consumer.
- *one-dimensional features*—which are the features that have the most impact on the satisfaction of the consumer; where the feature is present, the consumer will be satisfied, and where it is absent, they will be dissatisfied.
- *attractive features*—which are those features that are not required by the consumer, nor missed when absent, but which improve the satisfaction experienced by the consumer when present.
- *reverse features*—which are those features that the consumer does not want in the product. These are not flaws or problems, but rather excessive features that overcomplicate the product, for example, the prevailing trend to include cameras, mp3 players, video conferencing and internet browsing on mobile phones when the consumer simply wants a phone that makes and receives voice calls.
- *indifferent features*—which are those features that the customer does not care about, and which can be removed without the customer noticing.

The value of the Kano analysis is to determine what elements of the products are mandatory components ('must be'), which can be used to improve the value offerings (one-dimensional, attractive), and what can be removed to decrease cost and improve performance (reverse features, indifferent features). Details of the Kano measurement process are covered in-depth in Walden (1993, 1999) for those wishing to use the process in business.

Competition analysis

Competition analysis reintroduces several of the components used in the industry analysis, including the Porter Five Forces Model. Consequently the territory may feel familiar, however the competition analysis builds on the existing knowledge of the industry with a more focused approach tailored to dealing with specific opponents in the marketplace. The analysis section covered here deals with the process of identifying competitors, analysing the competitor, identifying the organisation's competitive position in the market and the role of market signals in competitor analysis.

Identification of competitors

Competitor identification holds to the truism stated previously—the shorter the comment in the book, the longer the process will be in business. It relies on the organisation understanding its own value offering to the market, the needs and wants of the consumer, and the structure of the industry. Consequently, it has been placed near the end of the analysis process to allow for the acquisition of this knowledge from the previous analysis processes.

Identifying the competitors for the organisation is a complex process that differs for each market, market segment and product/service offering presented to the market. However, the consistent element of competitor analysis is to judge competitors on the basis of the extent to which their value offering to the market can be used as a substitute for the organisation's value offering. By focusing on the value and benefit that the consumer received from the organisation, it limits the likelihood of competitor myopia. Competitor myopia occurs when the organisation can only identify current competitors or new competitors who resemble the organisation. For example, a broadcast television station with competitor myopia would only see threats from cable television or satellite television. Consequently, they would not identify value competitors who provide alternative entertainment outlets, such as DVD rentals, the internet or online distribution of movies.

Analysing the identified competition

Having selected a range of potential competitors to be analysed, the next part of the process is the actual analysis. Lehmann and Winer (1991) outline a four-step model:

1. Assess the current and future objectives of the competitor. To achieve this outcome, the organisation needs to be able to answer questions about its competitors such as:
   - What are the competitors trying to achieve?
   - Why are they trying to achieve this outcome?
   - Do the competitors appear satisfied with their achievements?
2. Assess the current strategy of the competitor. This assessment can be conducted by observation of the competitor, their products, promotional materials, distribution channels and so forth in order to be able to answer the questions:
   - What target markets are the competitors pursuing?

- What strategic focus do they appear to have?
- What are the elements of their marketing mix?

3 Assess the resources available to the competitor. This question will draw from the industry analysis undertaken previously, and from the organisation's own assessment of industry-wide resource availability. In addition, it will require the organisation to assess the competitor in terms of:
- What marketing culture is evident?
- What marketing assets are present? (See Chapter 4 for the marketing assets list.)
- What production capacity is evident?
- Do the competitors use the same suppliers and distributors as the organisation or do they have separate supply chains?
- What financial resources are available?

4 Use the first three steps to predict the future strategies of the competitors. This stage is a question of projecting the competitor's likely strategies, based on the organisation's assumptions of its competitor's resources, strategy and objectives. In particular, the organisation should look for issues such as:
- Does the competitor have underutilised resources?
- Are there any markets where the competitor is present but not operating at its full potential?
- Will the competitor be able to react to changes in the marketplace?

Information on competitors

All of the information needed for the analysis can be acquired from publicly available information. For example, by paying attention to the competitor's job descriptions during its recruiting phase, it is possible to determine if the organisation is expanding (new position in a new region), or what type of product development is taking place (recruiting specific skills). Broadly, there are five areas for information gathering on competitors. These are:

- *public information*—which can be taken from the competitor's advertising, its price, websites, annual reports and job advertisements.
- *trade information*—which is derived from third party publications including industry reviews, advertising magazines, and related trade press. For example, monitoring advertising and marketing trade press can determine when major competitors are likely to release their new campaigns. Similarly, if the competitor is in the process of replacing its advertising agency, it may be about to change strategy, or have suffered below expectation performance on sales or revenue.
- *government information*—such as industry reviews, annual reports and other information held through government departments, such as patents.
- *reported information*—which can include investor reports, annual reports, stock market information and investment prospectuses, all of which provide insight into an organisation in publicly accessible format.

- *internet information*—which can be sourced through Google and other search engines. Internet searching provides ample opportunities to discover competitor information. Use the advanced search function in Google to search the competitors' websites for Adobe Acrobat files (*.pdf), Microsoft PowerPoint (*.ppt) files or Microsoft Word documents (*.doc) to uncover competitor information. Similarly, Google can be used to research the backgrounds of the competitor organisation's key staff, CEO, suppliers or advertising agency.

Identifying competitive position

Competitive position is a combination of the abilities of the organisation (identified in the internal analysis), the opportunities present in the industry and the competition presented by the strengths and weaknesses of rival organisations. The components of competitive position are outlined in Figure 5.1.

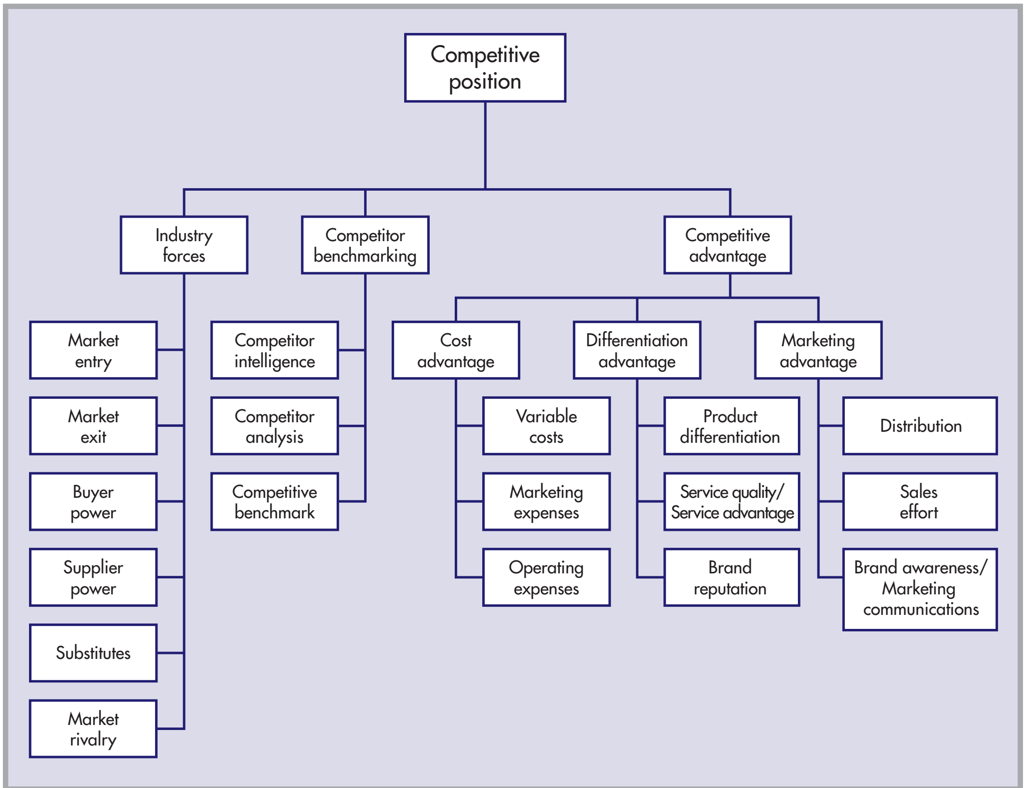


FIGURE 5.1 **Components of competitive position**

Competitive position is a complex looking task, which requires the accumulation and processing of a wide range of information. However, if previous analysis tasks have been completed in the internal and external analysis, the only new territory should be the competitor benchmarking.

Industry forces

Industry forces relates to the application of the information from Porter's Five Forces Model (which was covered in the industry analysis earlier in the chapter). Originally, the Five Forces Model was used to assess the influences present in the industry. In the competitive position analysis, the information from that preliminary analysis is now re-examined to discover areas of advantage and opportunity for the firm. In this context, the industry forces should be considered as a series of questions to review the value of each element for providing a competitive edge. The elements are:

- *Market entry*. What are the barriers to entering the market? Can these be raised or lowered by the organisation? Can a barrier be introduced to prevent competitors from encroaching on the market? How easy is it to enter the market and does this work to the advantage of the organisation?
- *Market exit*. How easy will it be to leave the market? Will entering the market commit the organisation to a potentially unprofitable venture that has to be maintained to satisfy the needs of key stakeholder groups? Does the organisation need to develop its own supply chains or can it use just-in-time arrangements to avoid overcommitting capital to the market?
- *Buyer power*. How strong is the customer in the market? Can the organisation increase or decrease the consumer's buying power? Will increasing the power available to the consumer adversely effect the organisation and its competitors? Can the buyer's power be reduced to increase the organisation's power over the customer?
- *Supplier power*. Can the power levels of the suppliers be altered? Can the organisation reduce the available number of suppliers with exclusivity agreements to decrease the market opportunities for competitors? Will engaging in just-in-time production increase or decrease the power the supplier has over the organisation?
- *Substitutes*. What level of product/value offer substitution occurs in the market? If the organisation is entering a market, how can it increase the level of substitution behaviour? If it is defending a market, can it reduce substitution with marketing relationships and relationship management? Is the organisation's value offering sufficiently unique to defend against substitution?
- *Market rivalry*. How competitive is the marketplace? Does an increase or decrease in the competition favour the organisation? What advantages can be gained from a competitive market (e.g. higher levels of consumer demand) versus a non-competitive market (e.g. stable market share)? Does the organisation have clearly defined rivals who can be used in the competitor analysis? Does the rivalry offer opportunities for positioning the organisation and its product offerings against those of a competitor?

While these questions are a starting point, they are not the only applications of the knowledge gained from the industry analysis. In general, the aim of the industry forces element is to ask how the influences on the industry can be used for providing a competitive edge to the organisation.

Competitor benchmarking

Competitor benchmarking is a three-part process based on the information derived in the competitor analysis above. The objective of competitor benchmarking is to develop the equivalent of a premiership or league table rating of the competitors in the marketplace. Whilst calculating a precise rating of 'first, second, third' is not necessarily achievable with the available information, a rating system of 'performing better, equal or worse' is an ideal charting mechanism across the range of competitive issues. There are three elements within each of the competitor benchmarks in the model:

- *Competitor intelligence*. This is the information known about the competition from the Lehmann and Winer (1991) analysis, competitor information, and the competitor market signals which are examined later in the chapter.
- *Competitor analysis*. This refers to the application of the outcomes of the Lehmann and Winer (1991) analysis to provide a series of comparison measures to assess the organisation's strengths, weaknesses and performance against its competitors. At this point the information from the analysis is used to generate the 'league table' approach along the key performance measures such as customer satisfaction, marketing assets, or parts of the value chain (Chapter 4, Internal analysis).
- *Competitive benchmark*. This element is an approach that views the processes of the organisation as modular units that can be compared with organisational groups within, and outside, the current industry. For example, the organisation's billing processes can be viewed as a modular unit, so that competitive benchmarking occurs against any organisation, in any industry, which deals with similar billing processes. The aim of the competitive benchmark is to look outside of the industry to acquire best practice from unrelated industries, for the dual benefit of improving organisational performance, and outperforming marketplace competitors.

For example, benchmarking training programs against similar training schemes in the same industry will ultimately lead to similar practices as the competitors. In contrast, taking a competitive benchmark from sports training can lead to process innovations and competitive advantages when applied properly.

Competitive advantages

Competitive advantage is the relative advantage the organisation has over its competitors. The advantage has to be meaningful to the consumer and it has to be sustainable against competitor's actions. Identifying a competitive advantage requires the use of the knowledge and information from the internal analysis (Chapter 4) with particular reference to value chain analysis (Porter 1985), customer analysis (Kaplan & Norton 1996) and core competency analysis (Prahalad & Hamel 1990). These elements represent the strengths and capacities of the firm, and can be used to rank the organisation's performance against its competitors. In addition, the competitor analysis also draws on the elements of the external analysis and customer analysis with reference to the perceptions of value. These are required to determine the competitive advantage as it relates to the value offering sought

by the consumer. Determining areas of competitive advantage is based on the organisation's ability to derive advantage from one of the following three elements—costs advantage, differentiation advantage or marketing advantage.

Cost advantage is the financial element of the process where the advantage comes from producing the value offering at a lower cost than the competitor, thus providing more revenue per unit for the same market price. This area is closely related to the financial analysis aspect of Kaplan and Norton's balanced scorecard. As illustrated in Figure 5.1, cost advantage consists of three sub-components:

- *Variable costs*. This component covers the manufacturing, transport and transaction costs involved in the creation of the value offering.
- *Marketing expenses*. This includes any expenditure on the acquisition or retention of the customer, and incorporates promotional costs, costs of retaining sales staff and other costs such as expenditure on marketing research.
- *Operating expenses*. These are the costs of the continued operation of the organisation, and are often outside of the control of the marketer. However, organisations with lower operating expenses (e.g. less staff, less warehouse overhead than competitors) will often be able to produce cost advantages.

Differentiation advantage is the relative superiority of the organisation's value offering to the consumer in one or more areas in comparison to the competitor's offerings. In order to qualify as a differentiation advantage, the value must be relevant and meaningful to the customer, and give benefit both to the organisation (differentiation advantage) and the customer (unique value). This form of competitive advantage draws on the value chain, core competency analysis and market needs to determine where the organisation can offer one of the following types of advantage:

- *Product differentiation*. This form of differentiation occurs where the organisation can deliver a value offering which is demonstrably superior in meeting the needs of the customer in an area such as reliability, performance, features, appearance or related factor. Determining a product differentiation advantage relies on information generated from the value chain, core competency, market analysis and customer needs market research.
- *Service quality/service advantage*. This type of advantage exists where the organisation can offer a superior set of personally deliverable skills and service performance that meets the needs of the customer. It is based on the same principles as product differentiation in that it needs to be valued by the consumer, and needs to be a sustainable advantage that cannot be easily replicated by the competition.
- *Brand reputation*. The third area of advantage is the social message attached to the organisation's value offering compared to the competitor's brands. Brand reputation is the end result of the marketing operations, but exists as a part of the differentiation advantage as an intangible component of the product.

Marketing advantage is the business advantage to be gained through the use of marketing techniques, and the ability to block the moves of competitors with superior access to communications, distribution or sales coverage:

- *Distribution*. This includes the distributor stakeholders, and the extent to which the organisation can gain a monopoly level control over the key distribution channels. With the advent of the internet, and direct-to-customer sales from manufacturers, the creation of a distribution advantage has become significantly harder.
- *Sales effort*. This includes the abilities and capacities of the organisation's sales force. It includes any exclusivity arrangements that can be made to block the sales of competitor products, along with the personal selling skills of the organisation's salesforce.
- *Brand awareness/marketing communications*. In this case, superiority is based on the ownership of the share of voice in a marketplace. This is measurable in terms of the ability of stakeholders and competitors to communicate alternative views to the market against those communicated by the organisation.

Competitive advantages are a complex and integral part of the overall goal and strategy setting for the organisation. In essence, the process of competitive position analysis is designed to give the organisation an understanding of what it offers to the market that is superior to the competitor, and how that offering can be used as part of a growth or value addition strategy.

Identifying competitor market signals

There are two types of market signals to be considered—overt signals and interpreted signals (Proctor 2000). Overt market signals are those obvious and deliberate actions by an organisation, which are intentionally performed to make the organisation's position clear to the market and industry. These include:

- *announcements of intention* which serve as a warning, threat or information to the competitors in the market. The prior announcement of business moves can serve the purpose of:
  - pre-empting the competitors by being first to announce their actions, if not actually first to market with their new product or strategy
  - threatening competitors with retaliatory actions if the competitor goes through with a planned action
  - testing the reactions of the competitors to proposed changes
  - attempting to reduce provocation and to avoid a price war by announcing and explaining decisions
  - defusing internal debate by public announcement of the proposed direction of the organisation
- *post-facto announcements* which include sales figures, annual reports or announcements of the marketing campaigns or market expansions which have been completed

- *public statements regarding the state of the industry*, and may involve engaging other organisations or the government in debate over the direction and future of the industry.

Covert, or implied, market signals are those messages that arise from the interpretation of the actions of the competitor. Caution must be used in dealing with implied market signals in that these are subject to the personal biases of the interpreter. However, certain actions by competitors can be interpreted as market signals, and these include:

- recourse to legal action against competitors
- the manner in which the competitor implements changes to its strategy and how consistent this is with previous activity
- divergence from past goals which can include developing radically new products, product diversification strategies, or sudden departures from highly-contested markets
- the 'cross parry' which is where Competitor A makes a move in market, and Competitor B defends by counterattacking Competitor A in a different market segment
- historical tendencies, which involves tracking the actions of a competitor over time to see if there is a specific pattern to its behaviour. For example, Pepsi-Cola had a propensity to flag when a retail prize promotion was about start by heavily discounting retail stock to clear the shelves to make way for the custom labelled promotional product. Similarly, Coke had a propensity to discount stock in October to create retail shelf space to launch the 'Summer' customised Coke bottles.

Understanding and recognising market signals is a part of developing an awareness of competitors and their actions. In addition, it can be useful for the organisation to assess what market signals its own actions are sending to the competitors, and to the marketplace. In the case of historical analysis, customers with trend-watching skills are able to quickly capitalise on the behaviour of the firm to exploit pricing trends or other obvious signals of change.

Business environment/macro-environment analysis

Business environment analysis brings in the broader spectrum of the environment stakeholder context, and draws together the issues associated with the macro-socio-economic environment in which the organisation and the industry exist. Defining the macro-environment is a question of excluding environment factors that have already been covered elsewhere in the analysis. For example, the organisation's competitors and customers can be considered part of the macro-environment, as can the state of industry, markets, distribution channels and supply chains. However, these factors have been addressed previously in other aspects of the external analysis process. Consequently, the business environment should be limited to those macro-environment factors that have not been covered elsewhere in the analysis.

The business environment defined

There are six consistent factors in the business environment, which are defined as:

1. *physical environment*—which relates to the geography, raw materials, infrastructure and other purely tangible elements of the business environment. For example, the physical business environment of the Northern Territory differs significantly from the environment of the South Island of New Zealand, and influences the types of markets, products and distribution strategies required. Analysis of the physical environment can be developed from knowledge acquired in the industry analysis, market segmentation and customer analysis. Similarly, it can also be used to assist the planning and development of geographic market segments based on the unique physical environment characteristics.
2. *economic or fiscal environment*—which relates to the state of the economy and includes factors such as inflation, unemployment rates, interest rates and related economic measures. Assessing the economic environment can often indicate trends in sales figures, for example, where interest rates are rising, discretionary expenditure is more likely to decrease, thus driving demand for 'luxury' purchases down.
3. *social or cultural environment*—which relates to the overall influence of the environment stakeholder context, and covers the social norms and societal expectations under which the organisation is operating. This is where the stakeholder needs of the local community, media, society, citizens and community groups are most influential.
4. *technological environment*—which refers to the growth and development of technologies in all industries and areas of society. This includes the increasing level of scientific debate in the media over issues such as nanotechnology, genetically modified foods or environmental issues such as global warming. The technological environment also encompasses innovations that directly impact on the organisation's industry (e.g. new processes for refining sugar) or broader changes such as the widespread adoption of the internet.
5. *political environment*—which encompasses the non-regulatory role of governments, social pressure groups and lobby groups. It is part of the broader stakeholder context of the environment as it can influence the actions of the organisation in responses to active social pressure and lobbying.
6. *legal and regulatory environment*—which includes government controls, laws and self-regulation.

Regulatory restrictions

There are three types of regulatory restrictions which impact on the operation of the organisation—government controls, self-regulation, and end-user regulation.

Government control

The most influential form of regulatory restriction is the role of the government at the local, state and federal levels in creating the legislation and regulations which govern the operational environment of the organisation. These range from the taxation laws—such as

the collecting and reporting of the goods and services tax (GST)—through to the limits and restrictions of the Australian *Trade Practices Act 1974* or the New Zealand *Commerce Act 1986*. For the most part, regulatory restrictions of importance to marketing strategies involve issues of fair trade (e.g. not engaging in misleading or deceptive conduct), or specific restrictions over the content of advertising (e.g. restrictions on the portrayal of violence in advertising in New Zealand and limitations on the demonstration of high speed driving in Australian advertising).

Self-regulation

The second area of regulation over organisations involves the voluntary compliance with self-regulation measures, such as the Australian Association of National Advertisers endorsement, and adherence to the standards set by the Advertising Standards Bureau. Voluntary industry regulation is a complex area involving balancing the needs of a range of stakeholders such as social pressure lobby groups, media, government and the broader community to demonstrate that the organisation, and its industry, does not require government regulation and control. In recent years, self-regulation has been under pressure as lobby groups attempt to influence the government to introduce laws to mandate the lobby group's self-interest. For example, the portrayal of high speed driving in advertising is currently self-regulated through the Federal Chamber of Automotive Industries. However, efforts have been made by lobby groups to attempt to outlaw the display of high speed driving in advertising. This follows the successful outlawing of the advertising and promotion of tobacco products by the *Tobacco Advertising Prohibition Act 1992*, which had previously been governed by self-regulated limitations on the timing and placement of pro-smoking content.

Controlling the consumer: end-user legal agreements

One of the newest mechanisms for regulation and control is the end-user legal agreement (EULA), usually found in software, but increasingly spreading to other products. The EULA is a legal mechanism rather than a marketing tool, and as a legal device, tends to list the limits of liability, the restrictions on use, and prohibitions on reverse engineering. It is important to consider that reverse engineering will occur where the financial gain for a competitor exceeds the risk of being caught, or where not reverse engineering the organisation's product endangers the ongoing survival of their organisation.

As a legal device, the EULA tends to caution against use innovation, and threaten penalties for using the product in a manner other than that prescribed by the organisation's lawyers. Whilst this can be necessary to defend against legal liability, the EULA is not a marketing device. In fact, where it prohibits use-innovations or aggressively limits the rights of the consumer, it can be seen as an anti-marketing device. Limiting the rights of the consumer may appeal to lawyers but should be seen as the antithesis of the marketing orientation—limits on rights reduces the value of the offering to the consumer. Reducing the value is contrary to the purpose of marketing strategy, and the efforts of a marketing-orientated organisation. Consequently, it is vital that the organisation assess the EULA applied to its product offerings to ensure that the marketing offering and legal restrictions are not conflicting.

Conclusion

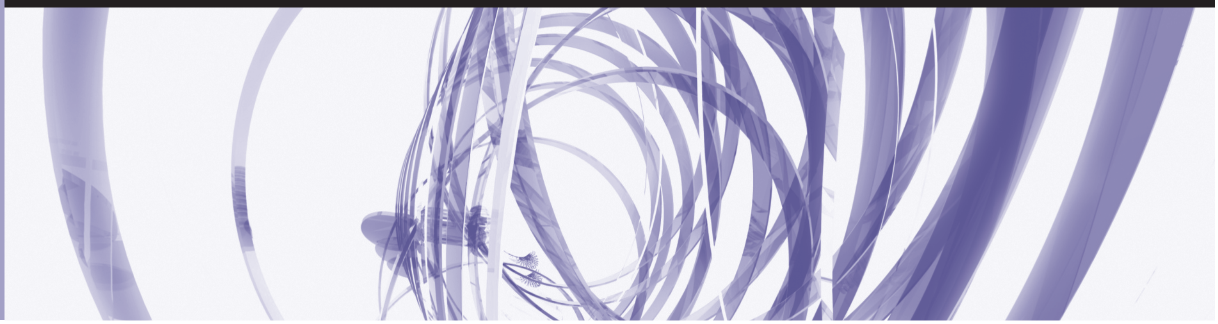
Undertaking the external analysis of the firm is a comprehensive process of analysing the available data on a wide range of influences including competitors, the needs and desires of the market, current and potential segments, stage in the industry life cycle, and regulatory environment. External analysis is particularly difficult to do well in practice due to the limited amount of quality information available on key variables. Competitor information, for example, is generally derived from a combination of secondary sources and observation after the competitor has taken a strategic action, rather than pre-empting competitor moves.

PART 3

Analysis into strategy

Strategic objectives

CHAPTER 6



Introduction

Chapter 6 examines strategic objectives as part of the development of competitive marketing strategy, beginning with the impact of market segmentation on strategic objectives. The chapter gives a broad overview of the types of objectives that provide overall strategic direction and which then lead to the use of growth, value addition or defensive marketing strategies.

Market segmentation

Segmentation is the method of dividing an existing market into manageable units. This is achieved by dividing the broad market on the basis of a series of variables to refine organisational focus on a specific sub-market that is considered profitable, viable and hopefully sustainable. Market segmentation is important as it underpins both market development and niche marketing strategies and provides the necessary focus to set specific business objectives for specific target consumer markets.

Steps involved in segmentation

Wood (2004) outlined a three-step process for market segmentation:

1 Choose a market

2 Apply a segmentation variable
3 Evaluate and select a segment.

Choosing a market

Market selection may already be in place as a result of the industry analyses outlined in the previous chapter. For example, suitable markets for segmentation can be derived from the industry life cycle analysis outlined in Chapter 5. This can be achieved through the examination of emerging and developing industries, and through the assessment of market needs of the mature market (Proctor 2000; Hooley, Saunders & Piercy 2004; Porter 1980). Similarly, the market attractiveness analysis in Chapter 5 used a specific market definition of how the organisation outlines its current and potential customers based on which needs and wants are being met or which could be met by a value offering from the organisation. Consequently, the definition used for the analysis could be re-used as the basis for the market selection for market segmentation.

This interconnectedness is a feature of the cyclical nature of the marketing strategy process—objective setting can contribute to the external analysis as much of it can draw from decisions in the analysis process. It all depends on the order in which the strategy setting process is conducted, the organisational history and the external forces impacting on the firm. In order to maximise the effectiveness of the strategy development process, organisations need to accept that there are areas of overlap, and then use this interconnection to their advantage rather than perceiving the process as a series of distinct and sequential steps.

Apply a segmentation variable

Kotler's (1998) basic 'who, what, where, when, why and how?' approach to market segmentation was mentioned with respect to the customer analysis phase of external analysis. At that point in the process, the aim was to gain as much insight into the customer as possible. Applying a market segmentation variable requires the organisation to use the information from Kotler's (1998) checklist to produce a series of specified market segments for evaluation and selection. Each organisation will produce a different series of answers to the checklist, and should therefore develop its own unique market segment concepts. Despite this variation there are consistent factors that need to be considered when creating market segments. These are encapsulated in the following questions:

- *Is there sufficient internal similarity amongst members of the segment to reasonably expect them to respond positively to the same marketing communications and value offering?* Internal homogeneity is critical to the success of a market segment. Homogenous segments will respond in a similar manner to marketing communication and marketing value offers, and targeted campaigns and offers can be focused on them. If individuals and groups within the market segment differ too widely in their response to the organisation's marketing effort, then the segmentation process needs to be re-done to create a more internally consistent market segment.
- *Is the segment heterogenous?* Segment heterogeneity is the extent to which the group of customers is dissimilar to other customers within the overall market. Since

most customers come from the same broad market, some degree of overlap should automatically exist. The purpose of assessing the heterogeneity is to determine whether the segment has been sufficiently developed to be different from the larger market. If the segment lacks heterogeneity, then it may present an opportunity for further division of the segment. An ideal segment therefore is homogeneous within the segment and heterogenous between itself and the market.

- *Is the segment clearly identifiable?* This question represents the extent to which the segment can be easily identified, targeted and addressed by the organisation. Given the purpose of marketing to create, communicate and deliver value to customers, customers have to be readily identifiable for this to happen. Segmentation variables should include identifiers—such as geography, psychographic or other measures—that can be used to target the delivery of the marketing message.
- *Is the segment measurable and substantial?* While the parameters of the segment are identified by answering the preceding question, for a segmentation strategy to be objectively evaluated, the size of the segment must be able to be calculated. Variables used as the basis of segmentation must provide some form of quantification, even where the basis is intangible and based, for example, on lifestyle variables. The requirement to measure the size of the market segment often results in a simple, easy to access measurement basis such as age, income and other demographic variables. Implicit in the whole market segmentation approach is the requirement that, having determined how many potential customers are in the segment, the company considers that there are enough probable buyers for the strategy to be profitable and contribute to a successful marketing strategy. Too tight a definition of the segment may lead to a clearly defined niche that is too specialised in its needs to be a profitable or sustainable market.
- *Is the segment accessible and sustainable?* Finally marketing strategists need to determine the ability of the organisation to reach the market segment through their communication and distribution strategies. It is possible to define and identify an ideal market segment that cannot be reached for some reason. For example, there are legal and regulatory issues governing sales of alcohol to the under 18s market. Whilst people in this market may consume alcoholic products, it is not viable for the organisation to develop a strategy to target them. Further the organisation needs to evaluate the extent to which it can repeatedly access and service the market profitably over time. If the nature of the market and the product is that a one-off sale is all that is likely to be achieved, rather than developing an ongoing commercial relationship through multiple sales or sales of complementary products, then the sustainability of the market segment needs to be questioned.

This process should result in a range of market segments being developed for use in the third step of evaluation and selection.

Evaluating and selecting a segment

The final step in the process is to rate each market segment across a range of factors, including several models from Chapter 2. For example, the Composite Portfolio Model can be used for rating the attractiveness of each market segment based on the organisation's competitive position and the perceived profitability of the segment. Similarly, if the organisation is already operating in the market segment, then the Directional Policy Matrix can be used in parallel with the internal analysis measures of the organisational resources.

The evaluation is designed to eliminate market segments that are not a suitable match for the organisation's needs or strengths. Once the number of market segments has been reduced to a workable number of profitable, sustainable or feasible target groups, these markets can be selected for use in organisational objective setting, market planning and strategy implementation.

A critical element in developing successful segmentation strategies is the willingness of the organisation to be ruthless in evaluation. All organisations face crossroads when hard decisions need to be made as to which of several equally attractive, potentially profitable but fundamentally incompatible segments they should focus on. The decision to reject a potentially profitable segment in the short term for long-term sustainable gain is always difficult. Ultimately the final choice of which markets to serve and which to reject is guided by the overall strategic objectives of the firm. As objectives are refined, segments which previously seemed attractive may lose their appeal. Specific marketing strategy objectives will follow from the decision as to which of the segments the organisation will focus on.

Segmentation, strategy and objectives

Segmentation is a central tenet of strategic marketing, and occurs at a number of points in strategy planning. For the purpose of this book, segmentation is placed prior to the setting of marketing objectives and after external analysis. However, part of the external analysis process requires the examination of market segments. Similarly, objectives can be set that require segments to be analysed and created, or alternatively, objectives can be set for each segment.

Segmentation is an ongoing and cyclical process whereby rough segments are created, evaluated, chosen, re-evaluated, retained or rejected, new segments created and so on. Objectives should be set for each market segment as appropriate, and any further refinement of the segmentation strategies should have occurred before, and during, the strategic processes covered in the following chapters (Chapters 7–13).

Setting objectives

Having identified preliminary market segments, the next step in the competitive marketing strategy process is to establish marketing objectives for the organisation. This section covers the nature of goals and objectives, the process of objective setting, and some of the common criteria that have arisen from business theory and practice for objective setting.

The language of competitive marketing strategy

There is no consistent use of the terms, with the same word having different meanings between different texts, articles and authors. Often, these meanings will change within the course of a book chapter, and sometimes within the space of the same paragraph. As there is no consistent use of the terms across the industry, this text will use the following meanings for the key words:

- *goals*—the purpose toward which an organisational endeavour is directed. These are the longer-term targets that are used to assist an organisation in achieving its overall mission.
- *objectives*—what the organisation intends to do or achieve. These are the shorter-term performance targets that lead to the achievement of the goals.
- *generic strategies*—the strategies used to implement the objectives are clearly measurable business behaviours that can be used as the basis for developing strategic and tactical marketing plans.

Understandably some degree of confusion will still exist when working with multiple texts and meanings. The definitions provided are consistent within this text, however, at times they may be inconsistent and in conflict with other strategy texts and articles.

Business objectives

Business objectives can be derived from a number of sources. Viljoen and Dann (2003) offer the broad spectrum approach of deriving objectives from opportunities, threats, strengths, weakness and stakeholders, a process which leaves few areas of business analysis untapped. Consequently, objectives can cover a broad range of areas from financial outcomes through to societal impacts.

In business, objectives can be set in a variety of ways. They can derive from organisational goals set by managers, from the board of directors, or in response to shareholder demands. Alternatively, objectives can develop as a result of systematically identifying opportunities from the internal and external analysis overviewed in Chapters 4 and 5. As with a large part of marketing and marketing strategy, there are no set objectives that can guarantee success in any given situation. Objectives need to be tailor-made for each organisation based on the needs of the organisation, its goals, capacity and the conditions of the market in which it operates. Although there are no guarantees, there is a series of general principles that have been distilled over time based on the experience of organisations worldwide and which can be used as a guide to objective setting.

Criteria for objectives

Whilst objectives can arise from a variety of sources, Cohen (2001), Wood (2004) and Viljoen and Dann (2003) agree on a series of criteria to maximise the effectiveness of an objective. These are:

- *acceptability*, which is the acceptance of the objective by key stakeholders. Internal acceptance of the objectives by other members of the organisation,

particularly those controlling the funding of the project, is essential for commitment. With the increased influence of stakeholders, acceptability of the objectives should also be matched against expectations of key external stakeholders such as local community or unions.

- *commitment inducing*, which is the level to which the objective is supported by other members of the organisation, both at the employee and managerial levels.
- *feasibility*, which is the extent to which the objectives can be achieved or fulfilled, and the level to which they are realistic. Practical, achievable and feasible objectives will inspire higher levels of commitment from members of the organisation than vaguely worded, idealistic statements.
- *flexibility*, which is the level to which the objective can be adjusted to reflect changed conditions. While objectives need a degree of certainty and concreteness, the organisation must retain the capacity to adjust to changed market conditions.
- *linked to organisational principles*, which is the extent to which the objectives are able to be traced back to the organisation's overall direction, principles and longer-term goals. This also includes the extent to which the objectives fit within the organisational culture of the senior management, board of directors and shareholders.
- *measurability*, which is the level to which the activities leading to the completion of the objective can be observed, measured and reported over a period of time. This includes having clear outcomes with set timelines and documented internal processes within the organisation to indicate what is to be achieved, by when and by whom. Measurability is examined again as part of marketing metrics in Chapter 15.
- *motivating*, which is the level to which the goal provides direction and drive for those people working to achieve it. Motivation is closely related to the acceptability, commitment, feasibility and participative criteria. Objectives need to be carefully balanced so that they are sufficiently challenging to inspire effort yet remain possible to achieve within the set timeframe and resource limitations.
- *participative*, which is the extent to which those involved in the implementation of the objectives have a say in their creation. Participative processes are useful for assessing the feasibility and acceptability of the objectives to the staff responsible for their implementation. Similarly, staff who are involved in the process of setting objectives are more likely to have a sense of ownership of the outcome, and are more likely to actively work to see that outcome achieved. Including the employees responsible for the implementation in the strategic processes of objective setting is part of the internal marketing of objectives and is invaluable for understanding and addressing employee concerns regarding the objectives and goals.
- *suitability*, which is the extent to which the objective matches the organisation's basic purpose and reason for existence. Suitability is closely tied to acceptability and the links to organisational objectives. This criterion relates to the broad

direction of the firm as set by the board of directors or shareholders. In contrast, acceptability focuses at the level of management, employees, and key external stakeholders.

- *understandable*, which is the extent to which the objective can be interpreted and understood correctly and consistently by all stakeholders. For many organisations, this will require multiple versions of an objective to be written in the appropriate style and language for specific stakeholder groups.

With the increased importance of the role of the organisation's stakeholders, and the benefit they are to receive from the actions of the organisation, it is important to consider the impact of the objectives on each stakeholder category. The interaction of the objective setting criteria and organisational stakeholders is summarised in Table 6.1.

Categories of objectives

Objectives can be clustered into broad categories based on the type of objective, the area of the organisation the objective involves, the likely types of outcomes, and the types of stakeholders who will be involved in those outcomes.

The eight categories are:

- *customer relationship objectives*, which include customer satisfaction levels, customer retention, account share, market share and relationship marketing objectives. These objectives are directly connected to the 2004 marketing definition as they represent the management of the customer relationship for organisational benefit (Kaplan & Norton 1996; Doyle 2002 and Viljoen & Dann 2003). This type of objective will involve the customer stakeholder, and those elements of the production context responsible for managing the customer relationship.
- *environmental objectives*, which are the objectives that directly relate to the use of the physical environment through land usage, energy consumption, air and noise pollution and environmental conservation factors (Viljoen & Dann 2003). This will involve the external environment stakeholders of environmental lobby groups and/or the local community.
- *financial objectives*, which cover the return on investment, and economic value added aspects of the organisation. This is the most universally recognised objective category for commercial organisations (Kaplan & Norton 1996; Doyle 2002; Viljoen & Dann 2003; Wood 2004). Objectives of this type impact on the stakeholder groups of financiers, shareholders and creditors.
- *innovation objectives*, which relate to the learning and growth capacity of the firm, new product development and information system availability (Kaplan & Norton 1996). These objectives require the involvement of most of the stakeholders in the production context (Chapter 3) with a particular emphasis on the employees and manager groups.

TABLE 6.1 **Objective criteria and organisational stakeholders**

Criteria	Stakeholder
Acceptability	Employees Managers Key external stakeholders such as unions, local community or the media
Commitment inducing	Employees Management
Feasibility	Financiers Employees Suppliers Distributors
Flexibility	Management Boards of directors
Linked to organisational principles	Board of directors Shareholders
Measurability	Employees Managers Financiers
Motivating	Employees Managers
Participative	Employees
Suitability	Board of directors Shareholders Financiers
Understandable	All key stakeholders involved in the delivery of the objective's outcome Any stakeholder to whom the objective needs to be communicated

- *internal business objectives*, which are related to operational objectives, internal business issues (such as quality), response time, cost and new production processes, and which involve the stakeholder groups of employees, suppliers and managers (Kaplan & Norton 1996; Doyle 2002).

- *marketing objectives*, which include adherence to the marketing orientation, the use of the marketing process and establishment of the marketing function within the organisation. This category is related to the customer relationship objective by virtue of the customer focus of the marketing orientation. However, the difference between the marketing objectives and the customer orientation objectives is the focus on the customer. Marketing objectives have an internal organisation-orientated focus on the use of marketing process whereas the customer orientation objectives have an external focus (Wood 2004). These objectives most likely will involve the management and employee stakeholder groups.
- *operational objectives*, which are based on meeting the needs of those involved in the production of the goods and services offered by the company (Doyle 2002; Viljoen and Dann 2003). Operational objectives are designed to facilitate the production processes, and may be considered both as an individual category of objectives, and a sun-objective of the internal business objectives.
- *social/societal objectives*, which are organisational objectives that specifically address the stakeholder needs of the local community and wider community, or aim to develop a non-financial social outcome for the organisation (Viljoen & Dann 2003; Wood 2004).

Several objectives overlap, for example the interaction between marketing objectives, internal objectives and innovation objectives. The purpose of presenting the eight generic categories is not to provide a rigid series of boxes to bind objectives as 'financial' or 'marketing'. Instead, the aim is to show how the commonality of purpose behind different categories of objective provides a framework, which in turn influences the behaviour of the whole of the organisation. Overlap and interaction is a feature of the model, not a weakness, since real-world organisational objectives do not readily fit into arbitrary categories.

Customer relationship objectives

Customer relationship objectives can be based either on the fundamental principles of relationship marketing or can be directly sourced from the results of core customer outcomes measures (Chapter 4). For example, the organisation could set objectives attuned to improving its level of trustworthiness with its clients, or to increasing its demonstrable commitment to the ongoing customer relationship through loyalty incentives for long-term customers. Alternatively, the results from the 5 measures of core customer outcomes can be used to form the basis of corrective objectives where necessary. In recap, the 5 measures are:

- *satisfaction*, which is the level to which the organisation is meeting the customer's needs
- *loyalty*, which is the intention of the customer to remain with the organisation, or to continue using the organisation's products to satisfy their needs
- *retention*, which is the level of success in maintaining the customer, and includes the costs of loyalty schemes
- *acquisition*, which is the process of acquiring the customer
- *profitability*, which is the difference between the revenue.

Objectives based on these performance measures can be set to raise factors such as profitability per customer through cost reduction, or to improve service for loyal customers to increase retention rates, satisfaction and loyalty levels. Customer outcome objectives are based on adjustments to the existing strategy and need to be judged against Doyle's (2002) disequilibrium concept. This concept states that increasing the satisfaction of one group comes with the risk of decreasing the satisfaction of another segment unless an equitable balance is achieved.

Environmental objectives

Environmental objectives vary by the size of the organisation and the nature of the value offering to the consumer. However, with the increased influence of environmental lobby groups, the organisation's interaction with the physical environment needs to be considered in relation to the broader organisational objectives. Viljoen and Dann (2003) include four sub-categories of the use of the physical environment in objectives:

- *land usage*, which includes the location of new facilities, shops, factories, and factors such as land usage for mining or harvesting raw materials. Objectives are often tied to other organisational objectives such as financial objectives of growth (for example developing a new retail outlet, or increasing market share).
- *energy consumption*, which includes the objectives of decreasing energy consumption during the production process, and may also include the potential impact of the product on energy consumption at the consumer level.
- *air, noise and environmental pollution*, which can arise from the creation, communication and delivery of the value offering. Noise pollution may arise from service delivery; for example, the establishment of a new retail centre in a residential area may increase the ambient vehicle traffic to the area, and increase the overall level of noise in the neighbourhood.
- *environmental conservation factors*, which include the physical impact of the disposal of the product, disposal of packaging and waste created during the communication and consumption of the value offering. For example, objectives can be set to develop recyclable or biodegradable shipping components to decrease the impact of packaging disposal. Similarly, objectives based on using targeted communications, rather than broad-sweep 'junk' mail outs, can reduce the environmental impact incurred in communicating the value offering to the customer.

For the most part, the environmental objectives are not seen as part of the competitive marketing strategy process. However, with the increased importance of stakeholders in marketing practice, attention to the impact of the organisation on the physical environment is becoming a marketing priority. In addition, specific physical environment goals based on reducing energy consumption, decreasing physical waste or improving recycling can be beneficial for both financial performance and improving the public image of the organisation.

Financial objectives

Financial objectives are the lifeblood of both for-profit and not-for-profit organisations and play a central role in the objective setting process. In the case of for-profit organisations, the ultimate aim is clearly to make a profit. For not-for-profit organisations, financial objectives are no less important as the organisation needs to achieve certain financial goals not only to provide its services to the target market, but to survive. The difference between for-profit and not-for-profit firms is in the emphasis rather than the existence of financial objectives.

Kaplan and Norton (1996) placed financial objectives as the top of a hierarchy of business objectives, alluding to the principle that the remaining objectives must correspond to the financial outcomes set for the organisation. The financial objectives category consists of:

- *profit*, which is the difference between the revenue gained by the outcome of the objective and the costs incurred to acquire this revenue. Profit is the overarching goal of commercial organisations. Within the overall profit orientation, however, it is possible to set individual objectives that do not result in an immediate profit, but rather result in tactical losses as part of a broader strategy leading to larger overall organisational profit. For example, selling hardware (colour printer) under cost price in order to establish a secondary market for profitable consumable goods (toner cartridges) is still a profit-driven objective, so long as the revenue from the consumables covers the losses on the hardware. In a similar way, not-for-profit organisations may set profit-oriented goals for some goods and services in order to cross-subsidise loss making elements of the organisation and therefore ultimately achieve their overall organisational goals.
- *return on investment*, which is where the objective is based on recouping the costs of investment over a period of time.
- *growth*, which is an increase in the size of market share, number of sales or other measure. Growth is often assumed to automatically lead to profits. However, to be financially successful growth objectives must arise from sustainable and profitable methods.
- *community service obligations*, which can include the financial burden of accepting unprofitable objectives for broader social objectives or as a trade-off between stakeholder needs and organisational goals. For example, an organisation may set an objective to continue to provide unprofitable services to a regional or rural community as part of a commitment to providing national service coverage.

Portfolio analysis and financial objectives

Portfolio analysis is useful in setting financial objectives by assessing which products are currently generating cash, and which have the potential to be cash earners later, even if they are not currently profitable. Hooley, Saunders and Piercy (2004) outlined three possible portfolio types:

- balanced portfolios
- unbalanced present-focused portfolios
- unbalanced future-focused portfolios.

The key financial objectives which arise from portfolio analysis are to redress an imbalance in the portfolio or take a calculated risk by deliberately creating an unbalanced portfolio. Unbalanced portfolios can be biased towards the present to take short-term cash gains at the expense of longer-term investments, for example exploiting a transient but highly profitable market segment at the expense of maintaining relationships with long-term clients. Alternatively, the objective could support increased investment in R&D, thus unbalancing the portfolio towards the future by risking short-term cash flow problems for a longer-term pay-off.

Innovation objectives

Innovation-based objectives are part of the Kaplan and Norton (1996) balanced scorecard. They are based on the belief that organisational self-improvement provides a means of providing improved productivity, efficiency and, ultimately, increased profitability. Innovation objectives are based on the subcategories of:

- *learning and growth capacity of the firm*, which is where the firm has structured objectives of improving productivity, product performance or other incremental development processes.
- *new product development*, which is based on the ongoing improvement of the organisation's value offering to the consumer. In this case, the objective is to sustain and develop improved methods of continuing to meet the needs of the consumer. By focusing on the needs of the consumer ahead of a physical product or a service solution, new product development can be a continuous process of innovation.
- *information system availability*, which are the objectives that are based on the incorporation of knowledge management systems within the organisation. This objective heavily involves the employee and the management stakeholder groups as sources of organisational knowledge. Objectives based on the capture of organisational knowledge also influence the level of information available for the value chain analysis, and for benchmarking employee satisfaction (Chapter 4).

Internal business objectives

Doyle (2002) and Kaplan and Norton (1996) both identified the categories of objectives that concern the internal business operations of the organisation. These types of objectives are based on changes to the organisation's behaviours for the purposes of improving efficiency or other factors. There are five subcategories of internal business objectives:

- *operational objectives*, which are based on the internal business processes that can be improved, enhanced, or used as a basis for sustainable competitive advantage.

- *quality objectives*, which are based on maintaining, raising or lowering the quality of the value offering. Although improved quality is assumed to be an automatic objective for all organisations, the quality imperative should be to deliver the quality level sought by the targeted customer group. A quality level beyond what is either expected or desired by customers leads to unnecessary additional expense and therefore decreased profits. By focusing on consumer-driven quality objectives a low-cost product can have its quality reduced to meet the consumer's expectations (low cost, low quality) rather than engage in the more risky processes of trying to change the expectations of the consumer or shift to a higher price.
- *response time objectives*, which are based on the speed with which the organisation can bring a new product or product modification to the market. Response time objectives can also involve the supplier and distributor stakeholders because as the organisation seeks to improve its responsiveness to the market, it will also require fast acquisition of supplies and quick shipment of final products.
- *cost objectives*, which are based on reducing the expenditure per value offering created and can occur through reductions in supplier costs, improvements in production process, decreases in product quality or other cost-saving measures.
- *new product processes*, which are based on implementing organisational learning, knowledge and innovativeness in the production of the organisation's value offering to the consumer. These types of objectives will involve employees, suppliers, management and possibly even the distributors as stakeholders.

Internal business objectives are closely related to the internal analysis processes outlined in Chapter 4 and the competitive analysis process from Chapter 5. In addition, internal business objectives are likely to have a direct impact on the product context stakeholders, in particular the employees and management, and also influence the suppliers (quality, cost and response time).

Marketing objectives

Wood (2004) highlights the marketing objectives of the organisation as a separate element from the international or operational processes. Marketing objectives are based on the implementation, maintenance and development of the organisation's marketing function, which occurs through:

- adherence to the marketing orientation
- use of marketing processes
- the establishment of an identifiable marketing function within the organisation.

In addition, the marketing objectives of the organisation are divided between the internal marketing and external marketing objectives. Internal marketing, including measures of internal marketing orientation, are covered in Chapter 15. External marketing objectives can be summarised as:

- the creation, communication and delivery of a value offering to the consumer
- the management of the organisation's relationship with its customers
- positioning strategies, integrated marketing communications and branding.

Within the context of competitive marketing strategies, the explicit recognition of marketing objectives as a separate category allows for the examination of the implementation of the marketing definition as a series of pragmatic objectives, rather than just merging the functional element into financial or operational objectives. For example, whilst the financial objective is 'profitability', the internal business objective covers 'cost' and the marketing objectives deal with the use of consumer behaviour theory to set the appropriate pricing strategy to be supported by the rest of the marketing mix.

Operational objectives

Operational objectives are the objectives based on the needs of the production context stakeholders, and involve setting objectives that assist in meeting the production needs (Doyle 2002; Viljoen & Dann 2003). These objectives can be derived from the information arising from having conducted a Porter Value Chain analysis (Chapter 4). Types of operational objectives include:

- *productivity objectives*, which are based on improving returns from expenditure or improvements in reducing the costs of operating the firm including the secondary components of the value chain. Return on the costs invested is not the same as reducing the costs—it is possible to increase revenue by increasing costs of production by spending more on higher quality parts, thus increasing sales by improving the product offering to the market to meet consumer expectations.
- *objectives designed to enhance competitive position*, which include those designed to increase market share, or to improve performance against key internal or key competitor benchmarks.
- *objectives based on employee relations*, which include objectives based on creating career paths, long-term employee commitment, employee satisfaction, and the development of employee skills.

Social/societal objectives

The final group of objectives are based on addressing the non-financial social outcomes for the organisation. Confusion may arise between the environmental objectives, which deal with the physical environment, and the social objectives, which deal with the environment stakeholder context. Social objectives are those objectives that are the explicit recognition of the influence of the stakeholder needs of the local and wider community (Viljoen & Dann 2003; Wood 2004). These can include:

- *participation in the local community*, which can be achieved through event sponsorships such as providing financial or other support to community events or local sporting teams
- *proactive involvement in social issues*, which includes job development, youth traineeships and support for disadvantaged groups in the local community

- *contributions to the social capital of the local region*, which is where the organisation actively attempts to improve feelings of trust, safety and community spirit. This can be achieved through objectives such as providing security for shared spaces such as malls or parks, or through sponsoring safety programs such as neighbourhood watch activities.

As traditional marketing communications channels become fractured and less effective, social objectives are increasingly integrated into competitive marketing strategies as organisations look for new ways to connect with consumers. For example, using local community services to provide support services to the organisation enhances the local community through job creation, increased disposable income, and a sense of community loyalty both to and from the organisation.

Objectives and stakeholders

Objectives themselves also can be seen to have distinct areas of interaction with the organisation's stakeholder groups. Table 6.2 outlines areas of possible interaction between the objective category and the different types of stakeholders.

TABLE 6.2 Stakeholders and objectives

Objective	Stakeholder	Primary context
Customer relationship	Customers	Consumption
Environmental	Social pressure lobby groups	Environment
Financial	Board of directors Creditors and financiers Shareholders	Production
Innovation	Employees Suppliers	Production
Internal business	Employees Managers Suppliers	Production
Marketing	Employees Managers Shareholders	Production
Operational	Employees Shareholders Suppliers	Production
Social/societal	Local community Media Social pressure lobby groups Society/citizens/community	Environment

As the table indicates, there is considerable crossover between the different objectives and the stakeholder groups. As stakeholder benefit is a crucial element of contemporary marketing, all eight categories of objectives now have an impact on the operation of marketing within the organisation.

Objectives and strategies

Strategies are methods for implementing organisational objectives in order to reach the desired financial outcome of profitability, return on investment or to deal with a community service obligation. Whilst strategies, like objectives, need to be tailor-made to each organisation, a number of generic strategies have developed over time to suit different generic conditions and intended outcomes. These strategies are derived from models such as Porter's Generic Strategies for value addition, and Ansoff's Growth Matrix. Other strategies have arisen from the Directional Policy Matrix (Chapter 2).

Generic strategies

Detailed analyses of the different generic competitive marketing strategies are covered in Chapters 7–13. For the purpose of this chapter, three divisions of generic strategies will be examined:

- *growth strategies*, which are objectives based on expanding the organisation's size, market share or range of product offerings (Ansoff)
- *value addition strategies*, which are the objectives based on improving the performance of the organisation through specialisation, value addition or tightly defined market segmentation (Porter)
- *defensive strategies*, which include maintaining market position or dealing with declining markets through harvesting or exiting the marketplace (Directional Policy Matrix).

The subcomponents of the three categories are summarised below.

Growth strategies

Growth strategies are based on Ansoff's Growth Matrix. Four types of growth strategies are addressed in the book. These are:

- *market penetration strategies*, where the organisation attempts to increase sales of existing products in existing markets (Chapter 7)
- *market development strategies*, where the organisation looks for a new market for its existing product range (Chapter 8)
- *product development strategies*, where the organisation brings new products to its existing markets by adding new features or alternative options and by developing entirely new products (Chapter 9)

- *diversification strategies*, where the organisation takes a new product to a new market, effectively producing simultaneous market development and product development strategies.

Diversification is usually implemented through the purchase or takeover of an existing company that has skills or products that fill a gap in the diversifying company's skills or product base. As such it is always a corporate-level strategy. While there are some strategic marketing implications arising from the implementation of diversification, it is beyond the scope of the marketing strategy. Consequently, diversification will not be dealt with in a separate chapter; rather, the issues arising from both market (Chapter 8) and product (Chapter 9) development should be considered when faced with a corporate strategy of diversification.

Value addition strategies—Porter's Generic Strategies

Value addition objectives are based on Porter's (1980) three Generic Strategies of business which are the:

- *cost leadership strategy*, which relies on the organisation being the business that provides products at the lowest feasible cost (Chapter 10)
- *product differentiation strategy*, which depends on finding a unique product offering for the customer and making this specific product offering profitable, sustainable for the organisation whilst ensuring that it is something the consumer desires (Chapter 11)
- *niche marketing strategy*, which relies on finding a market niche, and achieving domination in a particular market segment (Chapter 12).

Defensive strategies

The defensive strategies are drawn from the Directional Policy Matrix models such as the GE Matrix where the organisation has a poor match with the market and therefore lacks the capacity to fully exploit its investment. They are:

- *maintenance strategy*, which refers to the 'middle of the road' approach of dominating a weak market, or maintaining a weaker presence in a strong market as long as the continued presence remains profitable.
- *harvest strategy*, which is where the organisation plans a staged strategic withdrawal from a market. This is conducted by reducing the organisational commitment to the market whilst still attempting to maintain a profit margin on the product being withdrawn.
- *divestment strategy*, which is where the organisation exits the market after the product is deemed no longer sustainable, appropriate or desirable by the organisation.

Generic strategies and objectives

Having established generic strategies and generic clusters of objectives, the next step is to examine the interaction between the two areas. Table 6.3 outlines the generic strategies and their counterpart objectives.

TABLE 6.3 Strategies and objectives

Generic strategies	Objective
Growth	
Market penetration	Customer relationship
	Financial objectives
Market development	Financial objectives
	Operational objectives
Product development	Customer relationship
	Financial objectives
	Innovation objectives
Diversification	Financial objectives
	Innovation objectives
Value addition	
Cost leadership	Financial objectives
	Internal business objectives
	Operational objectives
Product differentiation	Customer relationship
	Financial objectives
	Innovation objectives
	Internal business objectives
	Operational objectives
Niche marketing	Customer relationship
	Financial objectives
	Innovation objectives
	Operational objectives
Defensive	
Maintain	Customer relationship
	Financial objectives
	Social/societal objectives
Harvest	Financial objectives
Divest	Financial objectives

There are three points to note about the interaction of objectives and generic strategies. First, financial objectives are the bottom line for each strategy. Whether the strategy is to divest a failing product line, or increase growth through new market and new products, each strategy relates back to the financial objectives of profitability, growth, and return on investment.

Second, not all of the objectives in this chapter are directly related to the generic strategies. Environmental objectives are not immediately connected to a generic strategy, although the sub-objectives, such as land use or energy consumption, may be influenced by market development or product development. Similarly, the marketing objectives do not have a corresponding generic strategy, although the use of any marketing strategy implies the adherence to the marketing orientation or the use of marketing processes.

Third, the purpose of Table 6.3 is not to bind a category of objectives to a generic strategy. Instead, the purpose is to demonstrate the interplay between objectives and strategies in order to examine each as a component of an integrated system, rather than as an individual isolated part. This is illustrated further by examining the cascading effect of integrating the generic strategy with its matching business objective, and the objective with its relevant stakeholder group. The end result is Table 6.4.

TABLE 6.4 Cascading effect—Strategies, objectives and stakeholders

Generic strategies	Objective	Stakeholders
Growth		
Market penetration	Customer relationship	Customers
	Financial objectives	Board of directors
		Creditors and financiers
		Shareholders
Market development	Financial objectives	Board of directors
		Creditors and financiers
		Shareholders
	Operational objectives	Employees
		Shareholders
		Suppliers
Product development	Customer relationship	Customers
	Financial objectives	Board of directors
		Creditors and financiers
		Shareholders
	Innovation objectives	Employees
		Suppliers
Diversification	Financial objectives	Board of directors
		Creditors and financiers
		Shareholders
	Innovation objectives	Employees
		Suppliers

Value addition		
Cost leadership	Financial objectives	Board of directors
		Creditors and financiers
		Shareholders
	Internal business objectives	Employees
		Managers
		Suppliers
	Operational objectives	Employees
		Shareholders
		Suppliers
Product differentiation	Customer relationship	Customers
	Financial objectives	Board of directors
		Creditors and financiers
		Shareholders
	Innovation objectives	Employees
		Suppliers
	Internal business objectives	Employees
		Managers
		Suppliers
	Operational objectives	Employees
		Shareholders
		Suppliers
Niche marketing	Customer relationship	Customers
	Financial objectives	Board of directors
		Creditors and financiers
		Shareholders
	Innovation objectives	Employees
		Suppliers
	Operational objectives	Employees
		Shareholders
		Suppliers
Defensive		
Maintain	Customer relationship	Customers
	Financial objectives	Board of directors
		Creditors and financiers
		Shareholders
	Social/societal objectives	Local community
		Media
		Social pressure lobby groups
		Society/citizens/community

TABLE 6.4 Cascading effect—Strategies, objectives and stakeholders (cont.)

Generic strategies	Objective	Stakeholders
Harvest	Financial objectives	Board of directors Creditors and financiers Shareholders
Divest	Financial objectives	Board of directors Creditors and financiers Shareholders
	Termination of customer relationship	Ex-customers

Competitor confrontation

One of the inevitable consequences of operating in a competitive marketing environment is the need to engage other organisations in the battle for market share and the consumer dollar. Kotler and Singh (1981) outlined a series of confrontation strategies based on conventional military tactics and converted into business options.

These six approaches are:

- *frontal attack*, where the organisation conducts an all-out offensive against a specific market or organisation. Frontal assaults are costly and require considerable resources. In addition, the clash of strength versus strength will usually require the organisation to absorb considerable losses as it attempts to out-perform the rival organisation in direct competition.
- *flanking attack*, where the organisation sets its strength against the competitor's perceived or actual weakness. Flanking attacks require considerable market intelligence and rely on the competitor analysis sections of the external analysis (Chapter 5). Segment-based flanking strategies can be deployed to assault a market leader from several angles, or the organisation can focus on moving from market to market without directly challenging the strength of the market leader.
- *encirclement attack*, where the organisation tries to cut off its rival's supply and/or distribution channels through exclusivity agreements, cut off access to the customers, or offer a product that is superior to its opponents' on all points of competitive advantage. Business strategies that rely on cutting off supply chains require sufficient resources to either acquire the supply lines or to be a more viable option as a single customer for the supplier than its current multiple customer market. Strong relationship marketing techniques, which increase the cost of breaking out of the relationship, can form an effective encircling tactic.

- *by-pass strategy*, where the organisation changes the rules of engagement through the use of technology to create new markets, or to take consumers from an old product (analogue watches) to a new product (digital watches) without competing directly with the existing product suppliers.
- *guerrilla tactics*, where the conventional strategies are set aside in favour of subtle, underground marketing efforts either to raid market share or to gain trial adoption by consumers of an existing product. This style of strategy is often used as a precursor to a larger movement in that the guerrilla tactics can weaken a business opponent and force them into defending market territory, and taking their focus off the main game.
- *non-confrontational tactics*, where the organisation focuses on its own customers, markets, value offering and value chains without directly launching an offensive on its market competitors. By focusing on becoming the best in the eyes of the market, the power of rival companies is reduced, albeit indirectly. This style of strategy is implemented through activities such as loyalty schemes, market penetration and customer satisfaction.

The different types of confrontation tactics are summarised in Table 6.5.

TABLE 6.5 Confrontation tactics

Tactic	Requirements
Frontal attack	Heavy resources
	Willingness to absorb losses
	One or more genuine competitive strengths
Flanking	Market intelligence
	Competitive advantage
Encircling	Dominant of supply or distribution chains
	All-round competitive superiority
	Relationship marketing and client exclusivity
Bypass	New technology
	Competitive advantage
	New product/new market
Guerrilla	Mobility
	Speed
	Unpredictability
Non-confrontational	Existing market share
	Existing customers
	Customer loyalty

In each of the strategy chapters, more specific detail will be provided on the nature of competitor confrontation for that chapter's specific growth or value addition strategy.

Conclusion

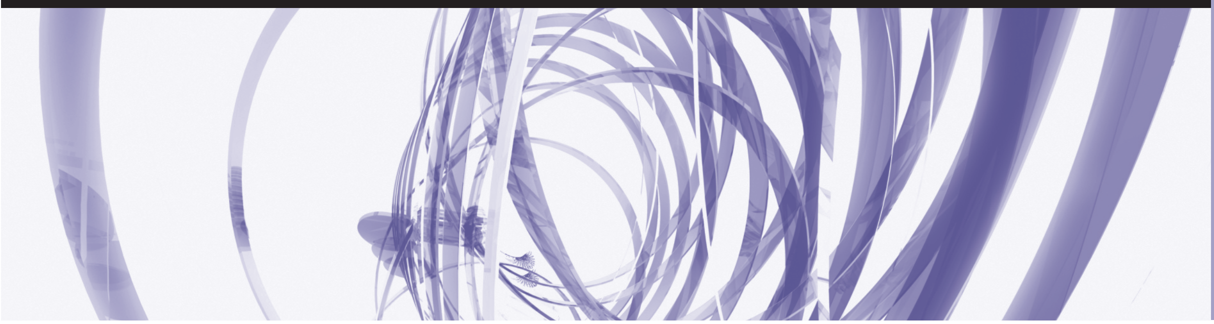
Long-term sustainable success is the result of developing effective and integrated strategies which bind the firm and its activities together. These strategies in turn are developed in response to clear and focused objectives. Given the complexities of the market and modern business, the process of objective-setting involves a wide scan of organisational needs, customer needs and stakeholder needs. Finding the commonalities amongst the needs of all groups and balancing the areas of conflict is the challenge of objective setting.

Objectives need to be set so that they are realistic, achievable and easily communicated to all stakeholders. While the objectives provide a framework for the organisation's activities and provide direction, they should not be so rigid as to be unresponsive to shifts in the environment and, most importantly, the needs and desires of the market.

This chapter has outlined how different organisational activities such as market segmentation impact on the development of specific marketing objectives. Further the chapter explores how different generic strategies such as growth lead to different emphases when objectives are being developed. When setting objectives it is critical to acknowledge the flow-on effect from one decision to another and to attempt to predict the likely impacts of each on the organisation, customers and stakeholders. While there is no single formula of the 'best' objectives for any given situation, the following chapters will discuss the different marketing strategy approaches which fall out of the decision to pursue one style of strategic objective over another.

Growth strategy 1—Market penetration

CHAPTER 7



Introduction

Market penetration refers to the strategy of growing the existing market and existing products. This is achieved either by getting more customers from the same target market or getting existing customers to patronise the company more often. This chapter focuses on customer retention, loyalty programs and relationship marketing strategies as a means of achieving market penetration. In addition typical changes to marketing mix tactics such as sales promotion and price discounting are discussed.

Tactical value of market penetration

Market penetration is often perceived as a low risk or 'easy' method of growth. As with most aspects of strategy, 'easy' is a very subjective statement. Viljoen and Dann (2003) note that the value of market penetration is that it requires minimal deviation from the organisation's current sales activities. Further, selling more products to existing consumers is usually perceived as a low risk alternative—the client is known, the product is known, and the market already accepts the value offering.

The risk inherent in this perception is two-fold. First, increasingly narrowing the organisation's focus to produce more of the same product for the same customers does increase

the risk of organisational myopia where the organisation can be 'blind-sided' by changes to the marketplace or the industry environment. Second, market penetration strategies deal directly with the core customer group, and the most valued sets of customers. If errors are made when addressing these markets, it will leave the organisation more vulnerable than errors made with non-core groups.

On the positive side, a market penetration strategy can be used to build on core competencies within a market to 'do what the organisation does best' and improve its brand reputation within a profitable market segment. As such, market penetration can be leveraged into brand leadership strategies (Viljoen & Dann 2003). Similarly, leveraging off competitive advantage in a known market is less resource-intensive than attempting to break into a new market, deliver new products to the market, or do both at once. The market penetration strategy increases the level of expertise the organisation has regarding its client base thus enhancing relationship marketing opportunities. It also creates opportunities for product development (new products to the existing market) or transferring the current successful product and its use innovations to a new market (market development).

Finally, the single largest factor behind the value of market penetration is its capacity to be successful and profitable. Controlling and adjusting market demand, sales and market response through the manipulation of brand management, pricing, packaging and promotion usually costs less than attempting to introduce new products to a new audience.

Ansoff revisited: assumptions of the market penetration model

Market penetration, the first of the four Ansoff growth strategies, is based on increasing the revenue from the current market, current customers and current product line up. As with all models, there is a series of preconditions that need to be present for the strategy to apply to the organisation. Market penetration assumes the following:

- existing markets and products
- ongoing customer retention
- the possibility of growth
- adequate supply of product
- growth is in the interest of the organisation.

Market penetration requires existing markets and products

This strategy assumes that the organisation has an existing market for the product. Any form of really new or quite new product cannot be used as part of a market penetration strategy. Consequently, product development as an integral element of a market penetration strategy is restricted to either use innovations (Chapter 6) or continuing products (Chapter 2). Similarly, any growth strategy based around acquiring new customers from outside of the existing market is a market development strategy. Market penetration may involve acquiring new customers, in that these are individuals who have not previously

used or do not currently use the company's brand. However these individuals must be part of the existing target market. In other words, the aim of market penetration is to extend the market share of the organisation in its current market or markets.

Market penetration versus market development

It should be noted that some aspects of market development are occasionally mentioned under the heading of market penetration. In particular, many strategy authors include entering new market segments as part of a market segmentation (Best 2005) or expanding a market to new users as part of the penetration strategy (Hooley, Saunders & Piercy 2004). For the purpose of this book, market penetration strategies are restricted to the following areas:

- increasing customer retention, improving relationship marketing and therefore increasing the lifetime value of the customer
- increasing volume, frequency or value of sales to the existing customer base
- finding new uses for the existing product amongst the existing customers
- increasing size of the share of the existing market by recruiting new customers from within the target market
- growing the size of the existing market by enhancing demand for the existing product (upstream marketing).

For the purpose of this book, the following aspects of market penetration, as reported by some other authors, are excluded from the operational definition:

- recruiting new customers from new market segments (market development)
- growing the size of the overall market by creating new demand in new markets for the existing product (upstream marketing, market development)
- use innovations that create new product uses for a new market (product development, diversification)
- creating new products (product development, diversification).

As with all areas of strategy and marketing, the practical implementation of a market penetration strategy will not be as clean-cut and easily pigeonholed. However, for the purpose of this text, the focus of a marketing penetration strategy will be on growth resulting from the sale of existing products to an existing market, and customers within that market.

Market penetration requires ongoing customer retention

The second assumption underpinning the market penetration model is that the organisation has and will retain customers. Under the current definition of marketing, the organisation is assumed to have a commitment to the ongoing management of the customer relationship. However, market penetration strategies require the existence of an identifiable group of current customers who will be recurring purchasers of the product. For such an approach to be effective, there has to be an identifiable gap between the level of customer retention due to what the organisation is currently doing, and what is possible if alternative marketing strategies are implemented.

The significance of this requirement is that it limits the use of the strategy to those products, services or ideas that require ongoing use—one-shot immunisation campaigns cannot use market penetration, however, annual influenza vaccines could make use of a market penetration approach. If the service is likely to be a single transaction encounter such as heart surgery, rather than a recurring transaction such as dental surgery, this form of growth model will not apply.

Market penetration requires growth to be possible

Market penetration strategies assume that an unmet demand exists in a market and that the consumer has untapped resources to spend, which means that it also assumes that market demand has not been met, or that the consumer can afford to purchase more units of the product. This is a significant limitation for the model where the product is in the maturity phase of the product life cycle (Chapter 2) or the market is in maturity or transitioning towards this phase (Chapter 5). It is also significant in that there may be a gap between what customers ideally want, and what they can realistically afford. For example, the target market may want to purchase a new car each year but realistically the best they can achieve is a new car every four years, irrespective of the quality of the firm's marketing and relationship building strategy.

Market penetration requires adequate supply of product

Related to the previous point is the capacity of the supply chain to deliver additional resources to support growth. Although the idea of market penetration-based growth is seen as a relatively simple process of increasing the volume of product that is consumed in the market, it requires complex calculations in the supply and distribution channels. This involves most of the stakeholders in the production stakeholder context, with a particular emphasis on the suppliers and distributors. Whilst the organisation may increase demand from the market, without adequate supply it cannot engage in a profitable growth strategy. Failure to meet the supply may hand a competitive advantage to a rival organisation that can service the demand the organisation created in its own customer base. Further, by raising expectations while failing to deliver on the promise, the strategy can have a negative long-term impact on the organisation, which ultimately leads to a loss of previously loyal consumers.

Growth based on market penetration is in the best interest of the organisation

The final assumption of the market penetration strategy is based on the Kaplan and Norton (1996) balanced scorecard where profitability is used as a central platform for determining the value of a given strategy. Market penetration-based growth needs to be carefully examined to ensure that increasing the flow of products to the existing markets will result in improved conditions for the organisation. For example, increasing the frequency with which the customer uses the services of the organisation may increase the overall cost of providing the service, in which case the capacity of the organisation to resource a market

penetration strategy is compromised. Similarly, increased service use may decrease the quality of service, or alter the consumption experience with long queues or less time spent per transaction. Given that the people most likely to experience the detrimental change in service quality will be the core customer base of heaviest users (usually the most profitable users), unchecked growth or poorly supported growth can result in the loss of valuable customers.

Core principles of market penetration-based growth

As mentioned in the definition of market penetration earlier in the chapter, the methods of growth covered by this strategy are:

- *customer retention*, which is the process of keeping existing customers through relationship management.
- *sales to existing customers*, which involves increasing the volume, value or frequency of sales to the existing customers.
- *use innovation*, where it is demonstrated that the product can be used for multiple purposes, which increases the rate at which the customer needs to repurchase the product.
- *increasing the share of the existing market*, which is the borderline between market penetration and market development. By recruiting new customers from the existing market, it remains part of the market penetration model, although recruiting new customers from new segments and new niches remains part of market development.
- *upstream marketing*, which involves increasing the size of the existing market through demand creation, or altering the conditions of the market.

Customer retention

Retention is separate from loyalty in that it represents repeat transactional purchases, or ongoing purchasing behaviour that is not part of a loyalty scheme. Retained customers may be behaviourally loyal but opportunistic and attitudinally neutral or negative. In other words, just because a firm or individual is a regular purchaser, positive attitudes and loyalty towards the company should not be assumed. Customers may buy from the firm simply because it is convenient, traditional or cheaper. Consequently these customers are very vulnerable to shifting to a new supplier should the new supplier perform in a superior way on any given decision-making criterion.

Whitwell, Lukas and Doyle (2003) present growth as a nine-stage sequential process starting with customer retention, and progressively increasing the ‘share of customer’. At the core of their growth platform is the need to retain existing customers at a higher rate than market competitors, and to gain customers at a rate higher than they are lost to attrition or other factors. Growth is assumed to occur where the number of new customers gained exceeds the customers lost, and the retained customers continue to be profitable.

The Whitwell, Lukas and Doyle (2003) model is most applicable in the growth to maturity phase of the product or industry life cycle, where the cumulative acquisition of customers presents a smooth gradient of consistent growth. Given the nature of the product life cycle, at some point in the process the growth rate will flatten out and decline. At this point, strategic customer retention is a defensive strategy. Discussion of this approach will recur in the defensive strategies chapter later in the book (Chapter 13). At this point retention is seen as a mechanism for aiding profitable growth and share of market.

Whitwell, Lukas and Doyle (2003) further outlined six keys to retaining customers, with the intention of converting the retention to customer loyalty and longer-term relationships. These steps are:

1. Select and prioritise customers
2. Customise the value proposition
3. Enhance value
4. Monitor satisfaction and loyalty
5. Follow up on complaints
6. Build customer partnerships.

1. Select and prioritise customers

The first step in a retention strategy is to assess the relative value of each customer against a series of benchmark criteria. Customer analysis has been discussed in relation to internal analysis (Chapter 4) and external analysis (Chapter 5). The information gained from these analyses should be used in the priority-setting process. Factors such as customer profitability, lifetime customer value and similar measures are discussed in 'Core customer outcome measures' (Chapter 4). For the purpose of market penetration, the emphasis is on prioritising existing customer groups from the internal analysis, rather than the potential customer groups identified in the external analysis. Customers can be prioritised based on the lifetime value models proposed by Berger and Nasr (1998) or through other metrics such as their perceived likelihood of buying additional products, or their level of unfulfilled demand.

2. Customise the value proposition

The second step in the process is the customisation of the value proposition. This is where the organisation adjusts the current product offering used by current customers to satisfy as yet unmet needs. This is not a value creation process as the product is already providing some level of value to the customer, which is evidenced by the customer having bought from the organisation in the first place. Rather it is value enhancement. As these are existing clients, the customer analysis process of examining the value offering being sought by the market (Chapter 5) should be easier and cross-referenced against the outcomes of the Porter value chain analysis (Chapter 4) together with customer feedback. Customising the value proposition tends to focus on the product and modifications to the product offer delivering the value proposition.

3. Enhance value

Modifying the value proposition to meet the needs of the market also has to result in the value offering actually improving or enhancing conditions for the consumer. As marketing consists of creating, communicating and delivering value, this is a core principle of the overall marketing process, as well as a key method of client retention. Value enhancement also requires the organisation to continually focus on needs being met by the value offering, rather than the product that is meeting that need. For example, focusing on 'personal transportation' would allow an organisation to move from selling horses to petrol driven cars to electric cars and beyond. Focusing on enhancing value allows the organisation to offer alternative value solutions in the form of use innovations. It can also be used to move from market penetration to product development where the enhanced value offering represents new product solutions to meet the same needs.

4. Monitor satisfaction and loyalty

Tracking satisfaction and loyalty amongst existing customers is conducted as part of the core customer outcomes of the internal analysis process (Chapter 4), and as part of customer relationship objectives (Chapter 6). Customer loyalty is seen by Whitwell, Lukas and Doyle (2003) as being influenced by satisfaction with the quality of the value offering, which in turn is affected by five factors:

- *reliability*, which is the extent to which the promised offering actually has the ability to deliver the promised performance
- *responsiveness*, which refers to the organisation's willingness to assist the customer, and to provide prompt and useful services
- *assurance*, which is the confidence the customer has in the employees of the organisation, and the trust which arises from the belief that the organisation knows what it is doing
- *empathy*, which is the level to which the organisation is perceived to care about the individual customer
- *tangibles*, which are the physical elements of the value offering, ranging from the product through to the presentation of the servicing employees or the physical facilities of the organisation.

The level of customer satisfaction with an organisation is influenced by the perceptions–expectations model. This model was developed in the services marketing literature but can be applied to the broader value offering. Perceptions–expectations theory argues that the difference between what a customer expects, and what they believe they receive, has the most influence on their satisfaction with the value offering. For example, if a customer expects poor service and receives adequate service, they will be more satisfied than if they expected a high standard and received adequate service. Although the two service levels are nearly identical, the gap between negative expectation and reality leaves the customer with a positive perception. In contrast, the service which does not meet the expected standard creates a negative perception.

Berry and Parasuram (1991) outlined five possible 'gaps' or 'break points' where the quality of the value offering can be undermined. The gaps are:

- *Gap 1: Misunderstanding customer requirements*, which is the gap between what the customer wants and what the organisation delivers as a value offering. This gap can be closed through increasing the value of the offering, customising the offering, or reducing customer expectations. It can be avoided by using quality market research in the first instance.
- *Gap 2: Poor specification of standards*, which is where the quality level offered by the organisation is below the expectation of the market. This factor is related to the problem of not understanding the needs of the customer. This gap can be addressed from information gathered in the value chain analysis (Chapter 4), the core customer outcomes analysis (Chapter 4), and the customer analysis process (Chapter 5).
- *Gap 3: Lack of capacities and capabilities,* which is where the organisation does not have sufficient resources committed to the delivery of the value offering to meet the needs of the consumer. This gap arises as a direct result of a growth strategy that increases demand on physical facilities or services beyond the capacity of the organisation to deliver. This is also related to Doyle's disequilibrium concept (Chapter 3). Whilst the shareholder can gain value from market penetration-based growth, the customer loses value if the capacities of the organisation are overwhelmed by that same level of growth.
- *Gap 4: Creating over-expectations,* which is where the organisation offers more than it can deliver, or promises an unrealistically high level of value satisfaction. Although this tends to be a gap experienced by first-time users of the product, it is important not to modify or offer to customise the value offering to a point where it creates over-expectation.
- *Gap 5: Misperceptions of the value offering*, which arise when the customer does not translate the service features (e.g. attentive staff) as benefits (individualised service) but perceives them as mis-features (annoying staff) or product failures (overly pushy staff).

These five potential gaps need to be examined closely when attempting a market penetration strategy as current customers are most likely to have the highest level of pre-existing expectations about the organisation's value offering. Market penetration growth strategies that result in reduced service quality or product shortages will have a significant adverse impact on satisfaction with the organisation since market penetration tends to target the high value customers on which the organisation relies to survive.

5. Follow up on complaints

The refocusing of the definition of marketing emphasises the management of the customer relationship. One of the most vital aspects of relationship management is the handling of complaints. Complaints should be treated as a form of market research which can be used

to assess whether a problem exists with the organisation's value offering. Dismissing complaints, or attempting to cover up the issues raised by the complaining party tends to lead to longer-term problems simply because the organisation is not addressing a perceived problem with its value offering. Marketing is about creating, communicating and delivering value. Where flaws are found in the value offering, these need to be addressed to ensure that the offering still meets the needs of the target market. Given that the objective of market penetration is to increase sales to existing customers, resolving the complaints of the customers is vital to the growth process.

6. Build customer partnerships

Customer retention is not equal to customer relationship. Once the customer is satisfied by the value offering, in that their expectations have been met or exceeded by the value offering from the organisation, efforts can be made to develop the relationship marketing components of trust, commitment and reciprocity.

Sales to existing customers

Retention is the key driver of selling more products to existing customers. Although the marketing definition focuses on relationship management, not all customers will want to engage in long-term relationships. However, customers who are satisfied with the value offering of the firm are likely to be retained, and the retention strategies mentioned in the previous section form the basis for the growth and expansion of the market. For example, managing the current customer's expectations of the product through the Berry and Parasuram (1991) gap model will assist in increasing the volume of sales to a market so long as the value offering is on the positive side of the perception–expectation equation. However, should the expectations exceed the perception of the value offering, the growth strategy will falter as the customer will become dissatisfied.

There are four methods of selling to existing customers, and these are:

- *increasing the volume of each purchase*, where the emphasis is on 'upsizing' the user to purchase more of the same product at each purchase, or a larger version of the product. For example, offering price discounting for volume can increase the size of the individual's purchase.
- *increasing the frequency of the purchase*, which is conducted through reminder advertising, or through repositioning the product into a higher-use category. For example, repositioning breakfast cereals as dry snacks for any time of day increases the rate of consumption and the frequency of repurchase.
- *increasing the value of the individual sales*, which is where the organisation attempts to bundle further products and services alongside the core value offering to the market. For example, this can be done through product bundling, where printer toner is bundled with printer paper, or through selling extra levels of insurance and warranty on products.
- *relationship marketing*, which is where the ongoing relationship with the customer is influenced by the relationship marketing principles (Chapters 1 and 2). This

involves developing trust, commitment and reciprocity with the customer so the customer becomes increasingly loyal to the organisation.

Sales to existing customers can be increased through longer-term strategies such as changing product use (two uses per day instead of one), or increasing the rate of use (use daily instead of use weekly). Shorter-term tactical gains can be made through price discounting, although that can lead to stockpiling which creates a spike of sales in the discount period and relatively flat sales at the full price. Finally, short-term promotions such as competitions or longer-term options such as frequent flyer miles or other loyalty programs can drive the volume and rate of purchase.

Use innovation

Use innovation occurs when the customer finds a new use for an existing product, thus creating a situation where they consume the product more frequently. Use innovations can be expanded from their original market into opportunities for market niching (Chapter 12) or can be presented as a new product use to a new market (Chapter 9).

Use innovation is identified through lead user analysis (Chapter 6). This is a four-step routine outlined by Best (2005), which is highlighted again here:

- Step 1: Identify lead users who have extended the use of the product
- Step 2: Study how lead users have extended the product usage
- Step 3: Discover how products could be modified to improve usage
- Step 4: Develop a more complete customer solution or new product.

Step 4 can branch use innovation out into product development (Chapter 9) or form the basis of customising or enhancing the value offer to improve levels of customer retention. Similarly, use innovation also involves the innovation adoption processes of continuing products (Chapter 2).

The value of use innovation for market penetration is that it increases the number of times the product is used, and the value the customer receives from the product. The flow-on effect should be that customer demand for the product increases since it provides greater value and it is consumed more rapidly as a result of these multiple uses. For example, white vinegar as a cooking component is used in small amounts and not at all in most recipes. However, when the same product is used as a cleaning agent, it is used more frequently and in greater volume. Consequently, consumers who use white vinegar as a cooking component and cleaning fluid will consume greater amounts than those who just use it for cooking.

Barriers to use innovations

Use innovations are one area where the needs of marketing may conflict with broader organisational needs and objectives. Whilst use innovation is usually perceived positively by marketing, modifying the end product for use in a manner not previously specified by the organisation may cause the consumer to run into conflict with the organisation's legal department. As mentioned in Chapter 5, conflicts between lawyers and consumers over the use of a product can be detrimental to the organisation's branding and may create

the potential for actual harm to be caused to the consumer, leading to claims against the manufacturer. The legal and other risks inherent in use innovation should be addressed as part of the overall business strategy of the organisation. The implementation of shrink-wrap licences, product disclaimers, digital rights management and 'Not for use in manner other than intended by the manufacturer' warning labels act as a deterrent to use innovation. The result of such legal limitations is that the organisation may lose business opportunities by tightly controlling what the market can do with its products. As with all strategy, the decision to encourage or discourage use innovation of products has to be balanced against the long- and short-term benefits of the firm and consistency with company objectives.

Increasing the share of the existing market

Increasing market share within the same market is part of market penetration strategy, and is the most common method of market growth in competitive or mature markets. This approach to market penetration assumes lower levels of customer loyalty to an organisation and its competitors and often focuses on fast moving consumer goods. The main approaches to acquiring customers from the current marketplace are based on:

- either matching or exceeding a rival's competitive advantage
- increasing the demand for the organisation's products ahead of those of its competitors (Proctor 2000).

Tactically this is usually achieved through measures such as promotional offers designed to get competitors' customers to trial, and hopefully adopt, the organisation's brand. For example, promotional offers can be based on discounting the price for a limited time, or by prize promotions as short-term measures. The expected outcome is that a percentage of those who trial the brand under the modified conditions will continue to use it. By acquiring this group of trial adopters, there will be an overall increase in the share of the target market.

Share Development Index

Market share expansion is based on the assumption that the organisation still has an untapped supporter base that can be accessed through the right combination of value offering and communication. Best (2005) offers a method of determining the likely level of opportunity available for organisations planning on developing their market share. The Share Development Index (SDI) is based on dividing the Actual Market Share (AMS) by the Potential Market Share (PMS) to create a percentage score of the organisation's market share performance. Low scores on the SDI indicate the potential for growth through the development of increased market share, whereas high SDI figures are indicators of dominant market share, which could be leveraged for increased revenue per customer.

Upstream marketing

The final category of market penetration is the non-traditional approach of focusing on upstream marketplace conditions in preference to downstream consumer use. Upstream marketing is based on increasing the total size of the market by improving the consumption

environment. Although it is not exclusive to market penetration, and although it may have greater value in market development or new product development, it can still be used in market penetration.

The focus of upstream marketing is usually on improving distribution channels. For example, successful lobbying of the government to deregulate the trading hours of supermarkets will increase the total number of customers who can access the store without the organisation offering a new product or tapping into a new market. Similarly expanding the availability of branded soft drinks by increasing the number of vending machines available and improving the quality of vending machines to accept notes and cards as well as coins, increases the opportunity for the current customers to consume drinks at different times and places leading to an increase in overall market share.

Competition and market penetration

Market penetration is the most subtle of Ansoff's growth strategies, and as such, is most likely to slide beneath the competitor's radar. The subtle nature of increasing sales to existing markets also makes it one of the hardest competitor strategies to counter. Consequently, the competitor analysis from Chapter 5, and the knowledge of the competitors from the environment stakeholder context, become important factors in being able to counter a rival's market penetration strategy. Without detailed knowledge of a rival's usual strategies, the shift towards market penetration may be difficult to detect. Table 7.1 outlines the match between the confrontation tactics (Chapter 6) and the market penetration strategy (Chapter 7).

Market share gained by market penetration tends to be focused around non-confrontational techniques such as increasing sales from existing customers. However, as marketing relationships between buyer and seller progress, they take the form of encircling tactics as the increasing costs of breaking the relationship effectively cut the consumer off from a competitor. In contrast, increasing market share through the use of matching a rival's competitor advantage can be seen as a frontal assault in that the two organisations are competing head to head on their competitive advantage strengths.

TABLE 7.1 **Competition, strategy and tactics**

Technique	Tactic	Offence	Defence
Customer retention	Encircling Non-confrontational	Customise the value proposition Enhance value Increase satisfaction Increase loyalty Improve quality	Competitive advantage Price competition Alternate value offering
Sales to existing customers	Non-confrontational	Increase volume of sales Increasing frequency of sale Increase value of individual sales Relationship marketing	Product substitution Competitive advantage
Increasing share of market	Frontal attack Flanking Guerrilla	Competitive advantage Increasing demand for product Positioning Pricing Competitions and promotions	Matching or exceeding rival's competitive advantage Relationship marketing
Use innovation	Bypass Guerrilla	Patents Customisation and enhanced value Communication of use innovation to market	Patents Use innovation specific product marketing
Upstream marketing	Bypass	Collaboration Lobbying Industry Alliances	Collaboration Lobbying Industry Alliances

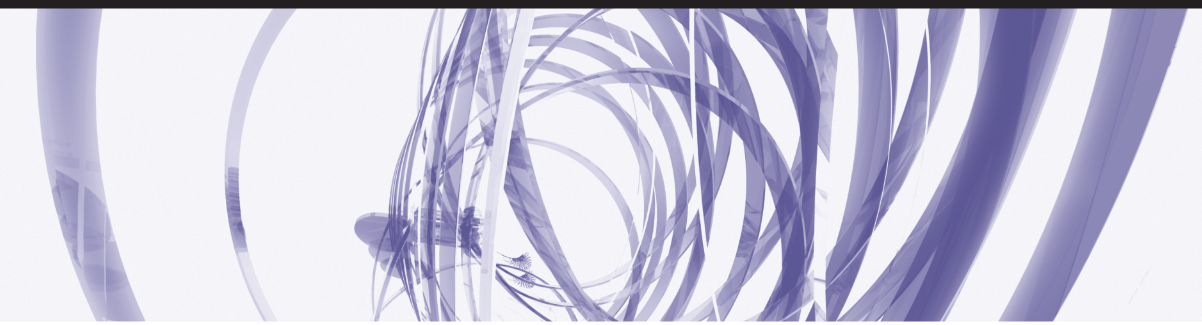
Conclusion

Market penetration is often perceived as the simplest, lowest-risk growth strategy available to the firm as it deals with two known variables: the existing marketing and existing products. Based on the notion that growth can be achieved by getting the existing target market to use more of the existing product offerings, the decision to grow through market penetration is underpinned by one of two key assumptions. Either it is assumed that there is an unmet demand for the product within the target market, or that consumers are prepared to move to alternative suppliers. Market penetration strategies are often used for relatively low cost, low involvement products such as fast moving consumer goods like soft drinks. It is also an appropriate strategy in the services marketing area where the development and maintenance of quality relationships with clients can lead to increased use of the service.

Market penetration strategies tend to be less confrontational than market development strategies. Due to the subtlety involved in getting more use from an existing client base, for example through variations to loyalty programs, it is often difficult for competitors to recognise or react to the strategy until it is well established. One point that is important to remember when engaging in market penetration strategies, however, is that there is a significant risk inherent in being too focused. Over-reliance on existing products and consumers can lead to a form of business myopia whereby larger trends in the environment representing fundamental shifts in consumer preferences may be overlooked, as the company fights out market share with competitors in an ever-decreasing market.

Growth strategy 2—Market development

CHAPTER 8



Introduction

Growth through market development involves the creation and development of new market segments for the firm's existing products. Market development strategies for transferring existing products into new market segments and for the development of international markets are discussed. The chapter also features the multi-step 'New Market Development' framework designed to assist in the implementation of market development strategies. Finally, it overviews the range of competitor influences on the introduction of an existing product to a new market in which a competitor is already supplying products.

Tactical value of market development

Market development occupies the middle ground between market penetration and product development in terms of perceived risk. By using an existing value offering as the basis for growth the organisation can make use of its knowledge of the product, economies of scale and other related benefits that accrue with experience with a product. By further building on existing value chains and organisational knowledge, the size of the market can be extended substantially without having to commit to a radical restructure of the firm, and without the introduction of possible conflicts with new product lines.

In addition, the broadening of the market base for a product offers a level of protection against sudden changes in market conditions. By spreading the revenue stream from being dependent on a smaller group of heavy purchasers to a balanced portfolio of customers across markets and industries, the organisation decreases its vulnerability. One of the key disadvantages of the market penetration strategy compared to that of market development is the dependence on the same core group of customers for both regular income and increased growth.

However, market development is not without risk. It does rely on introducing a perceived new product to a market with which the firm has limited experience and which has limited experience of the firm. Whereas minor modifications to the value offering in market penetration are continuous products, the organisation may find itself delivering a perceived dynamic or discontinuous innovation to its newly-selected markets, whilst selling the same 'old' product to its core audience. Differing perceptions as to the novelty of the product mean that customised marketing strategies need to be employed in different markets. In effect, the decision to engage in market development forces a multiple segmentation strategy onto the firm with all the risks and benefits inherent in such an approach. Strict control over communication within each market is required to maintain the relative position of the product with both old and new consumers.

Reasons for market development

Whitwell, Lukas and Doyle (2003) outline three stimuli that drive the organisation towards seeking new markets for its existing products. These are:

- the opportunity to build synergy with existing knowledge and value offerings
- newly emerging high-growth markets which present viable and competitive opportunities for the organisation
- the desire to move from a niche market to the broader marketplace.

The common thread of the three stimuli is the organisation's desire to take its value offering from a smaller group to a larger group of customers.

Ansoff revisited: assumptions of the market development model

Market development strategies are based on expanding the existing user base by acquiring new customers from new segments. Implicitly market development requires the existence of a current user base as the starting point for the expansion. The market development strategy model is based on the following assumptions:

- the organisation has an existing product for new markets
- the organisation has an existing market for the product
- the organisation can access the new market and supply the existing product to it
- profitable and sustainable growth is possible through entering a new market.

Existing products for new markets

Core to the strategy is the use of an existing product for a new market, in contrast to product development, which requires new products for old markets, or diversification and niching, which require new products for new markets.

There can be some confusion in regard to whether the pre-existing product is an 'innovation' or not. From the organisational perspective, an existing product is not an innovation when it is introduced to a new marketplace. However, the same value offering will be perceived as 'new' or 'innovative' by any market segment with no prior experience of the product or competitor products. For example, Krispy Kreme doughnuts are an established product in the US, but a 'new' style of snack for the Australian market. The product itself is not an innovation for the firm but is perceived as such by consumers in the new market.

Existing markets for the existing product

The second point reinforces the need for the organisation to have an existing market that uses the value offering. An organisation which has an existing product which is being introduced to a new market is effectively no different to one introducing a new product to a new market. In addition, aspects of the market development process are dependent on the behaviour of the existing market. For example, developing new markets through the transference of use innovations from one market to another requires the initial group of consumers to use (and innovate with) the current product. Although this seems obvious and logical, if the value offering being suggested for use in a market development strategy does not have a current market, the most appropriate application is to use either product development or diversification strategies.

Accessibility and supply

Market accessibility is a key assumption behind a growth model based on taking an existing product to a new area. Accessibility in this respect is a multi-layered effect, including factors such as:

- *geographic access*, which is the ability to deliver the product to the market.
- *supply chain logistics*, which includes the ability of the current suppliers to deliver the necessary components to the organisation. This becomes a major factor when examining expansion into international markets, as 'international' suppliers may be needed to replace the current 'local' suppliers.
- *distribution channels*, which is the mirror twin of supply chain logistics in that the organisation needs to be able to deliver its value offering to the market. If the organisation is targeting global markets, then multiple layers of distribution can often increase the final price to a level that makes it difficult to compete profitably in the new markets.

Profitable and sustainable growth is possible in the new market

The underpinning rationale for expanding the organisation's market presence is to create sustainable levels of growth and sales in the new marketplace. In other words, growth via expansion into a new market is not the sole objective in itself, rather it is a means to an end. Although growth is not the prime indicator of a successful market development strategy (as ultimately all growth strategies are aimed at improved financial success) in the case of commercial operations, it is often the easiest facet to measure. Market development is a preliminary step towards converting a market segment from a non-user group into a loyal group that can be sustained with market penetration strategies. Consequently, markets which are strategically developed on the basis of a loss per customer need to be limited, particularly if the loss is likely to rise per customer as the share of the market increases.

All growth strategies require a level of financial success to ensure the ongoing survival of the organisation. The creation, communication and delivery of value to this new group of customers is done for the benefit of the organisation, usually in the expectation that initial losses will be recouped in a given time frame and the segment will move from being unprofitable to profitable. Loss-making segments are usually only consciously developed and maintained as a limited defensive strategy to prevent the expansion or introduction of competitor organisations into the market.

Core principles of market development-based growth

Market development is based on duplicating an existing value creation process for the purposes of customising, communicating and delivering that value offering to a new market (Proctor 2000). There are four broad methods for implementing a market development strategy. These are:

- using market segmentation (Chapter 5 and 6) to refine new target segments from the existing industry or market (new segment, same market)
- growing total market share through acquisition of related niches and segments (related niche, same market)
- expanding the overall market demand (upstream, same market)
- global expansion with existing products (new market).

These are based on the research of Best (2005), Viljoen and Dann (2003), Whitwell, Lukas and Doyle (2003) and Wood (2004).

Revisiting market segmentation (new segment, same market)

Market segmentation is the key to a market development growth strategy. In order to have a series of targeted markets that can be systematically addressed with the organisation's value offering, the company must have completed a series of market segmentation studies.

Segmentation is the method of dividing an existing market by a series of sub-factors such as demography, psychographics, geography, predicted or actual sales figures (Chapters 2, 5 and 6). One of the critical aspects of market segmentation in a market development strategy is that it relies heavily on the external analysis (Chapter 5) to provide the requisite information for selecting and prioritising market segments.

As noted in Chapter 5, market segments are often selected first, then analysed, then refined and re-selected for further review. Consequently, the cyclical nature of the process provides an advantage for market development based strategies, as change in the market can be used to identify new potential users of the product. Broadly, market development based on revised market segmentation looks at the market segments identified in the initial analysis that led to the targeting of the current market. It may be possible to identify new potential markets by reassessing those markets that were similar in priority to the current market, that were not initially optimal or profitable, and that are now viable targets. Similarly, the priority rankings for unrelated markets may have also changed, based on the revised situation of the organisation in that the current product may make these unrelated markets more or less attractive.

Finally, since one outcome of market development is a stable situation where market penetration becomes the most viable growth strategy as the organisation gradually acquires the 'new' segments, more related and parallel market segments may become available for market development.

Acquiring related niches (related niche, same market)

Whitwell, Lukas and Doyle (2003) and Proctor (2000) identify the sideways movement of the organisation from niche to niche across an industry or larger market as an ideal method of market development. Addressing parallel or related niches provides the organisation with a series of benefits:

- possible synergy between the existing and the closely related, but not identical new markets
- the opportunity to combine smaller niches based on psychographics into larger segments based on usage
- prior experience with similar customers, which can assist in modifying the positioning of the product.

The key disadvantage of the sideways movement across a market is the cross-contamination between the related niches where the 'new' niche has vicarious experience of the organisation's value offering, and has rejected it. Similarly, modifications to the value offering in parallel, but still separate, niches may unduly influence the organisation's reputation in a core market. For example, as the market development strategy expands the user base of the organisation, changing the branding or altering the price for the new market will impact on the existing users. A price-based promotion designed to encourage new users to the product may only serve to allow existing users to bulk-purchase at

discount, and may not result in significant gains in the new market. Alternatively it may lead to feelings of frustration on the part of the core users who then become less brand-loyal, and more likely to switch to a competitor in protest.

Related niche market development can also be seen as a deliberate strategy to use when trying to move a new product from the innovator adopter phase through to the early adopter or early majority phase (Chapter 1). In practice, innovators are a form of specialist niche. They are the initial adopters of the product, but do not provide sufficient revenue for the long-term survival of the organisation. By learning from the innovator's experience with the product, it is possible to adapt the value offering to the broader market of early adopters. Not only does this provide a continuous innovation for the organisation to sell to the early adopters, it presents an opportunity to commercialise any use innovations created by the innovator class, and to correct problems arising from the early versions of the value offering.

Geographic segmentation as related niches

It is possible to use market development as a deliberate method of compensating for a limited product release during the introduction of a new product. If the organisation cannot secure sufficient supply and distribution chains to service a wide market distribution, they can focus an initial distribution on a geographic niche (e.g. releasing only into a capital city in one state). This can be coupled with a projected plan of implementing a geographic related niche market development strategy to grow the organisation organically across the country as it progressively gains sufficient supply and distribution channels. Developing a systematic geographic growth campaign also provides the organisation with opportunities to integrate its planned growth into the objectives of its supplier and distributor stakeholders.

Upstream marketing and market demand (wider market)

Upstream marketing has been defined previously in Chapter 3 as the process of manipulating the environmental variables, market conditions and market needs by targeting the level above the consumer (Goldberg 1995). Consequently, upstream marketing presents an opportunity to the organisation to increase the size of the overall market, which should theoretically increase the number of customers and market segments that are available to all of the organisations in the market, assuming that the organisation maintains or expands market share. This also presents opportunities for industry-level partnerships and alliances whereby organisations and their suppliers cooperate with the aim of expanding the overall market. For example, Microsoft and Intel focused on upstream marketing to increase the number of computers of all types being used, working on the assumption that the increased spread of personal computing will increase the demand for Microsoft products and Intel-equipped computer components. Similarly, the most recent spate of upstream marketing has come in the form of industry lobbying to increase the volume of internet-based services provided by banks and the government. By creating an upstream demand for internet access to use online government services, the computer industry has increased the overall size of the industry for PC products, and each expanded their own markets.

Going global (new segment, international market)

Globalisation and the accompanying factors of international markets and export industries represent a variation on the geographic market development. International markets are often deceptively similar to domestic markets, but contain subtle and usually commercially fatal differences. George Bernard Shaw is purported to have described England and America as 'two countries divided by a common language' which, in the modern global marketplace, could just as easily be described as 'two markets divided by a common brand'. Globalisation as an extension of the market development strategy needs to be carefully monitored to ensure that the value offering for the global market does not require so much localisation as to make it a new product for a new market. Similarly, barriers of communication, even when technically in the same language, can limit the extent to which the organisation can communicate and deliver its value offering. Finally, Simmonds (1999) cautions that organisations need to have successfully handled their national strategy and their national markets before entering into an international context.

Issues in market development

The core principles of market development are based around the application of the existing product to a new market and include:

- adjusting for the 'old' product being a 'new' innovation
- working through the 'new market development' process, which is based on the new product development framework
- lowering the barriers to entry on the new markets.

Old to new: innovations and market development

Market development and product development create diametrically opposite situations for the organisation. In Chapter 9, the emphasis will be the creations of products that are new to the organisation, and are new from the organisation to the market, but which may at the same time be 'old' products in a marketplace. For example, an electronics firm that creates clock radios and expands into delivering electric toasters will have a 'new' product by creating the toaster. Toasters themselves, however, will be old news to the market.

In contrast, market development creates the potential for the reverse situation where the 'old' product in the organisation can be a 'new' product for the specific market segment. In this respect, the clock radio manufacturer that introduces its product to a new market will be delivering a form of innovation to the marketplace, but dealing with an old technology in its own organisation. Consequently, both the internal and external perception of the value offering need to be assessed to ensure that the organisation is positioning the value offering to the market in a way that reflects the perceptions of the market, rather than organisation's internal view of the product.

TABLE 8.1 Market and organisation perception of the product

		External view to new market		
		Continuous (same product)	Dynamic (improved product)	Discontinuous (new product)
Internal organisational view of the product	Continuous (old product)	Market development	Market development	Market development
	Dynamic (modified product)	Market development	Market development/ Product development	Product development
	Discontinuous (new product)	Product development	Product development	Product development

In Table 8.1 there are nine possible positions that the product can hold based on the newness of the product to the market and organisation. Five of the positions are relevant to the product development growth strategy, and will be discussed in Chapter 9. The remaining positions relate to the organisation/market perception of the product and are:

- *continuous–continuous*, which is where the organisation is aware that the product is not a new invention to the new market, but has been a part of the organisation's product line. Positioning within this market is based on showing the continued match of the product's benefit to the needs of the consumer. The focus in this situation is to portray the organisation's product as superior in meeting the needs of the market when compared to existing competitor products that are already in that particular market. Competitive advantage can therefore be derived from extending a reputation or brand across new geographic markets that had been restricted by supply or distribution problems. For example, a regional store with limited range of stock which expands the available stock due to improved shipping will be offering continuous–continuous innovations (known products to the store chain and customer) but will be part of market development if this was part of a broader plan to access regional geographic markets.
- *dynamic–continuous*, which is where the organisation may run the risk of believing that they have a 'new' or 'improved' value offering to present to the new market, and the new market perceives no difference between the current products already available and the recent arrival. This is where close attention to detail in the competitor analysis (Chapter 5), competitive advantage (Chapter 4) and the Kano Method (Chapter 5) become vital in determining organisational strategy. If, after objective and critical analysis, a clear competitive advantage or point of

differentiation exists, then the market development strategy needs to focus on communicating this to the market. If no advantage is present, then the organisation either needs to abandon the market expansion, or revisit the product offering to match the needs of the market.

- *continuous–dynamic*, which is where the arrival of the organisation's product in the market is seen as an improvement over existing value offers, or an upgrade to the current market conditions, even if the organisation regards its product as 'old'. This may occur in the case of customer driven use innovations where the organisation sees its 'product' as a series of features, and the customer sees it as a series of solutions.
- *continuous–discontinuous*, which is where the organisation's 'old' product is a brand new solution to the market. Historically, this type of perception gap has been the most common method of entering a new geographic market, especially any international market. Competitive advantage in this type of market situation is based on first mover advantage, although this is only a transitory phase. Success from being first to market can often indicate to a larger competitor that the market is worth entering, in which case the organisation needs to emphasise a competitive advantage based on needs solutions, rather than being 'new'.
- *dynamic–dynamic*, which is where the modifications to the organisation's product offering bring it in line with the needs of the market and create a new solution for the customer. This is most commonly seen where technology upgrades offer new capacities and solutions to the market as the organisation modifies and updates its value offering. Positioning under these market conditions should be based on emphasising the 'and improved' aspect of the 'New and improved' value offering, since the customer perceives this product to be an improvement on the existing solutions in the market rather than a new concept. This type of market condition also gives rise to the 'second mover advantage' where the later arrivals to the market can bring copy-cat products that fix the problems with the original value offering.

It is possible for a product to occupy multiple positions in the grid based on the market and the organisation. For example, duct tape is one of the world's most adapted products, giving it a high level of use innovation, and consequently a propensity to be used in a wider range of markets than 3M may have originally intended. The product was designed as a repair mechanism for creating temporary seals. However, due to use innovations, the product plays a role in everything from its intended use in emergency repairs through to modern fashion <www.ducttapefashion.com> or simply taping multiple objects together <www.ducttapeguys.com>. Had 3M focused on the product (a roll of tape) rather than the end-user solutions (applying tape to people, objects and unusual circumstances), it may have missed the opportunity to expand the market for tape into human repairs—3M now offers a duct-tape band-aid under its Nexcare subdivision <www.ohgizmo.com/2005/09/30/the-duct-tape-band-aid>.

Model of new market development

The framework used in the decision-making process involved in bringing a new product from an idea through development and into implementation can be adapted into use for selecting, reviewing and developing new markets.

The New Market Development framework consists of six major steps:

- *target acquisition*, which is the initial decision to expand to a wider series of markets
- *preliminary market screening*, which is the first phase of examining the fit between the current product and the new potential markets
- *business analysis*, which is the formal process of estimating expenditure required to enter the market, and the likely financial reward
- *market development*, which is the process of adapting the existing value offering and the supporting market mix for use in the new market
- *test marketing*, which is the preliminary roll-out of the product to a small subset of the broader market
- *full roll-out*, which is a staged conversion of the new market to an existing market that can be used for a follow-up market penetration strategy.

Target acquisition

Target acquisition can arrive from multiple sources within the organisation, although the use of the service staff as listening posts is one of the better methods of sourcing potential new markets. Front line staff can observe the sale of the product, and are most likely to uncover use innovations in their interactions with the customer. Organisations intending to use a market development strategy should investigate the implementation of knowledge management systems tailored towards the acquisition of information regarding how the customer actually uses the product. Best (2005) outlines four types of markets to consider for developing new targets. These four are:

- *related new markets*, which has been mentioned extensively throughout the chapter, and would qualify as one of the easiest and most successful methods of expanding the user base. The related markets approach is where the organisation examines similar types of markets in the nearby geographic region, or comparable markets that were identified in the initial market segmentation process.
- *unrelated new markets*, which are often entered through acquisitions at the corporate strategic level that are outside of the control of the individual marketers. Entering unrelated markets can also arise as a result of the external analysis, particularly factors such as the market attractiveness analysis or competitor analysis. Choosing to enter an unrelated market is a high-risk strategy, and can border on the implementation of a diversification strategy. Alternatively, unrelated markets can be seen as those international markets where demand for the product is identified, but where the organisation has no history with the country.

- *new developing markets*, which represent the decision to examine areas of rapid growth in an industry (technology) or region (China) and offer existing products and services where those products meet a common need in the new market. With the recent acceleration of technology market growth, and the subsequent widespread distribution of advanced technology, new developing niche markets arise more quickly, and tend to be easily identified. For example, even in the halcyon days of the dot-com bubble, the dot-com start-up companies still needed office suppliers, accountants and finance products, all of which were existing products supplied to a rapidly developing new market.
- *underdeveloped existing market*, which is where the market has been restricted by law, or has not, in the opinion of the organisation, reached its potential. This may be an area where upstream marketing can be used. Upstream marketing is used to simultaneously 'unlock' or improve the condition of the existing market, whilst the organisation also offers its current products to the customers in the same region or market segment. For example, mobile phone manufacturers could promote government deregulation of the personal mobile phone market to increase the number of suppliers who would want to sell a mobile phone product. Similarly, supplier and distributor stakeholders can use upstream marketing to create demand for the end user products that will translate into a maturing of an underdeveloped market, thus creating more opportunities for them to service the organisations competing in the marketplace.

Preliminary market screening

Preliminary market screening occurs when the organisation returns to models such as the industry attractiveness analysis (Chapter 5) or Directional Policy Matrix to assess the organisation–market fit (Chapter 2). Market screening is effectively a method of taking the short list of new potential markets, and prioritising them in the same fashion as a market segmentation strategy (Chapter 6). As with market segmentation analysis, the organisation may have to decide between short-term losses for long-term gain, or short-term options with limited long-term viability. In order to make this type of business judgement, the organisation should make use of the balanced business scorecard and the portfolio analysis (Chapter 4). Given that it will have finite resources, limited time and incomplete information, these conceptual models may not be able to provide definitive answers. However, working through the elements of the new market development model as part of the market screening process will assist in understanding the nature of each market, which will in turn assist the business analysis process.

Business analysis

At the core of the business analysis step for the new market development process is the dual question of profitability and sustainability. Whilst other analytical frameworks such as internal business issues, customer relationships and pursuit of innovation should be factored into the analytical process, each of these parts of the balanced scorecard point to the bottom line of financial returns.

In contrast to the new product development technique (Chapter 9), new market development has the advantage of being able to draw on existing organisational information regarding the value chain, profitability and cost structures of the current product. As the organisation has already invested in the infrastructure, production capacity and organisational learning, the business analysis should be centred on increasing the profitability and return on investment from taking the current product beyond the boundaries of the core market.

Market development may indicate that the core product has been sufficiently successful to warrant expanding its involvement with the market. Further, if the business analysis is examining related or parallel niches, much of the information from the original internal and external analysis may be able to be reused to determine the financial viability of the new markets.

Market development

Having selected one or more markets to develop, the organisation then needs to return to the market segmentation analysis once more to confirm that each segment conforms to the checklist outlined in Chapter 6. The five key questions to answer are:

- Is the segment homogenous within?
- Is the segment heterogenous compared to other segments in the market?
- Is the segment clearly identifiable?
- Is the segment measurable and substantial?
- Is the segment accessible and sustainable?

With these five questions answered in the positive, the next step is to develop the individual marketing plans for the different segments.

Best (2005) outlines a list of factors to consider when developing individual plans for growing market demand and developing a market. These are:

- *price*, which is a factor when considering the total cost of the product to the new user, including aspects such as time spent learning to use the new product, risk of embarrassment of being the first (or last) to have the new product, and the actual cost of the product. Price is a difficult aspect to balance as the initial temptation is to reduce financial price to encourage adoption, however any pricing change for the new market will inevitably have to be reflected in pricing for the core customer groups. Similarly, the price needs to reflect the positioning of the product in the original market segment, and in the new segments. Offering a luxury ‘prestige’ product at a discount trial-adoption price will irrevocably damage the brand in both the core and expanded markets.
- *interest*, which is the extent to which the product has the attention of the potential user, and to which it will provide the new market with a series of benefits not already present in the market. Interest is composed of the actual benefits the consumer derives from the product, the perceived competitive advantage

the offering has over its rivals, and the communicated messages from the organisation to support these two factors. This is also related to the issues in Table 8.1 regarding the organisation and market perception of the newness of the product.

- *compatibility*, which is the level to which the new product fits the market, either by providing a series of solutions to wants and needs, or by being appropriate to the social conditions. Compatibility ties in with the analysis of external stakeholders in the environment context, and the specific organisational stakeholders identified as key influences in society. Compatibility also relates to how well the product will fit the use situation and will be able to be used to satisfy the needs of the market. For example, whilst distributing high quality wine in cans will meet a specific need for transporting measured quantities of drinks to dinner parties it may not be suitable for the actual use situation. Traditionally, wine has not been served by ripping the tab off a can. Further, the appearance of the canned wine in packaging similarly to drinks sold to young adults and children may also conflict with the broader societal expectations of not encouraging under-age drinking.
- *availability*, which is tied into the supply and distribution issues discussed throughout the chapter, and involves the supplier and distributor stakeholders. This is the implementation solution to the segmentation question of whether or not the market is accessible. Market development-driven growth cannot occur in the absence of a distribution and delivery mechanism that can deliver the value proposition to the market in a timely and cost-efficient manner.
- *awareness*, which is the extent to which the segment is aware of the new product. Awareness and interest are inter-related. Although it is possible to be fully aware of a product and not interested in the features it offers, it is not possible to be interested, yet unaware. Awareness is also the first stage in the product adoption process, and should be considered the most basic component of the plan for developing a market. The customers need to be aware of the existence of the new product, but the organisation must not fall into the trap of believing that simply knowing about the product will automatically lead to brand loyalty and repeat purchase. Assess the extent to which the customer is aware of the product, and the level of interest that they have in adopting the organisation's value offering. Once awareness has been achieved, focus on converting interest into action and actual purchase rather than continually re-informing the market of the existence of the product.

Test marketing

As with new product development, some degree of test marketing is recommended before the full product roll-out commences into a new market. Unlike the testing of a product, the testing of a market automatically contaminates the targeted marketplace, as once a firm has entered the market, knowledge of the firm and its products cannot be systematically withdrawn. Given the nature of social networks and word of mouth activity, a focused

approach to testing only a limited proportion of the market to gauge its reaction, will not necessarily lead to information about the organisation's strategy and intended entry into the market being confined to the original test group.

Consequently, market research in the form of focus groups and laboratory tests is a more practical solution than isolating a sub-segment of the new market for testing. Using modelling techniques it is possible to form educated conclusions as to the viability of the new market and the likelihood of the firm's success.

Full roll-out

The final step in the process is to actually implement the marketing plan and to deploy the existing product into the new market. During implementation, the focus is on moving the customers from their 'new market segment' status to being part of the market segment of 'current users'. As mentioned previously, one objective of market development growth is to create more users of the product who can then be targeted with a market penetration campaign.

International market development

Expanding from local into international markets is an obvious and common form of market development. International marketing is a distinct sub-discipline within marketing theory and practice and as such, any discussion in the broader marketing strategy context is necessarily brief and superficial. Many texts and journals exist which specifically deal with the complex issues involved in international marketing and should be consulted by those who choose to pursue this option.

In brief, from a strategic perspective the major benefits for organisations entering the international market are the potential to reach significantly larger numbers of potential customers and the potential to develop unique marketing mixes which are less likely to be cross-contaminated by existing market segments, than occurs in the case of market development within the same geographic space. International market development allows the organisation to be innovative in its positioning and communications strategies, allows for significant price variations within product lines without incurring negative feedback from existing domestic customers, and allows alternative distribution strategies which will not adversely impact on perceived positioning in the core market. For example, a product which is fairly common and perceived as everyday in its home market, may acquire additional status due to country-of-origin effects when sold into new international markets. Consequently whilst the product may be relatively cheap and distributed widely through chain stores in its country of origin, in the new international market it may be positioned as more of a prestige product with limited distribution and relatively high prices.

Despite these benefits there are significant problems associated with entering new international markets. Key among these are the lack of existing distribution networks and strong relationships with international stakeholders, and the potential to misjudge

the demand for, or reaction to, the marketing strategy due to misperceptions of culture. Distribution is the key to success in developing new markets. Although there are some commonalities, each country will have differing distribution networks, key stakeholders, legal issues surrounding the distribution and sale of different classes of products, different expectations of relationship building and so on. One of the most common causes of failure in international market development strategies is the inability to break into these complex systems of networks and relationships.

A second key issue is the need to fully understand the local culture, restrictions within the culture and the informal, social rules which govern the sale and promotion of goods and services. Whilst market research is valuable in uncovering some of these issues, there are numerous stories that highlight the failure of companies to understand local market conditions, which consequently results in a successful product and campaign from one country totally failing in another.

Increasingly, small- to medium-size firms are taking the international market development option. Much of the impetus behind this is the increasing access to previously difficult to reach markets via the use of the internet and web-based distribution strategies. The types of product most suited to international distribution via the internet are those which are fundamentally information-based. Included in this category is any product or service that can be reduced to a digital format and can therefore be easily transmitted online for a fee. Music, software and research are three major product categories which have allowed small to medium firms to successfully access new international market segments via the improving online technologies now available. Online marketing also allows individuals to bypass many of the restrictions inherent in traditional export activity.

As with international marketing, internet marketing is a specialist field of marketing and those interested in adopting this strategic approach to market development, particularly on an international basis, should consult specialist advice. Whenever an organisation decides to adopt a market development strategy which involves developing a new international market or market segment, specialist local advice should be sought.

Barriers to new market development

There is a series of common barriers for organisations entering a new market, not least of which is that an existing market will have existing competitors, and the organisation entering a market will automatically be in conflict. Unless the organisation is providing a discontinuous solution where no other organisation was providing a product alternative, entry to the market is an automatic frontal or flanking assault on the competition.

Best (2005) identifies three key barriers to market development strategies, which are:

- *lack of market access*, which is the fundamental break-point on any market development strategy. However, market access is a vital part of market segment

selection and the new market development process, and is an underpinning assumption of the entire strategy.

- *technology requirements*, which range across the gamut of the organisation's production capacity and can include access to the production facilities to mass-produce the value offering in a format that can be distributed to the new market. Similarly, technology barriers can work in reverse where the organisation's value offering is based on the need for minimum technology levels (e.g. electricity) or a specific technology (Java-based mobile phone) or minimum end-user skill level (literacy).
- *cost of entry*. Although the new market development process does suggest alternatives to a purely financial focus on determining entry to a new market, the bottom line is that market growth needs to be financially sustainable and profitable.

Certain markets may be inaccessible due to the costs associated with servicing the market. The cost of entry may be countered by a re-analysis of the organisation's cost structure, re-examination of the value chain or seeking financial aid from government to 'break into' the new market. Caution should be exercised if the cost of entry into the market remains high and the organisation is relatively late to the market, as this should be factored against its market attractiveness. However, if the cost of entry is likely to remain static, and will provide a natural barrier to competitors entering the market, it may be worth pursuing for a newly developing market. Upstream marketing may also be used to attempt to lower barriers—for example, a highly regulated marketplace has a higher cost of entry than a deregulated alternative. Understanding the nature of the barriers to successful market development is as important as understanding the opportunities. Marketing strategy needs to simultaneously lower the barriers while maximising the potential of the opportunities.

Competition and market development

Market development can be very confrontational. By entering new product into an existing market, there is a strong chance that the organisation will be in direct conflict with other existing products in that market. For example, in the previous chapter, the emphasis was on customer retention and loyalty building. By entering an established marketplace, the organisation will need to counter its competitors' retention strategies with the new product offering, and then retain the newly acquired customers. Of course, it is worth noting that the newly acquired customers have demonstrated that their loyalty extends to the point of pricing, competitive advantage or product superiority which indicates that the people now forming the initial core of the business's share of the market are in fact the least likely to engage in loyal customer behaviour. Table 8.2 summarises offense and defence strategy for market development.

TABLE 8.2 **Competition, strategy and tactics**

Technique	Tactic	Offence	Defence
New segment, same market	Frontal attack Flanking Bypass Guerrilla	Competitive advantage Positioning Pricing Competitions and promotions	Matching or exceeding rival's competitive advantage Relationship marketing
Acquiring related niches and segments	Frontal attack Flanking Guerrilla	Communicate the value offering to related market segments Produce a competitive advantage Increasing demand for product	Matching or exceeding rival's competitive advantage
Global expansion with existing products (new market)	Frontal attack Flanking By-pass Guerrilla	Increasing demand for product Increase size of industry and market segment	Product substitution Counterattack the 'home' market of the international organisation
Upstream	By-pass	Collaboration Lobbying Industry alliances	Collaboration Lobbying Industry alliances

Conclusion

Once an organisation dominates a particular market or niche, a common growth strategy to employ is that of market development. Market development involves taking the existing products with which the firm is familiar, and marketing them into a new market or market segment. Consequently it appeals to organisations that are comfortable with their existing product range, have some reputation or actual product advantage and can benefit from economies of scale.

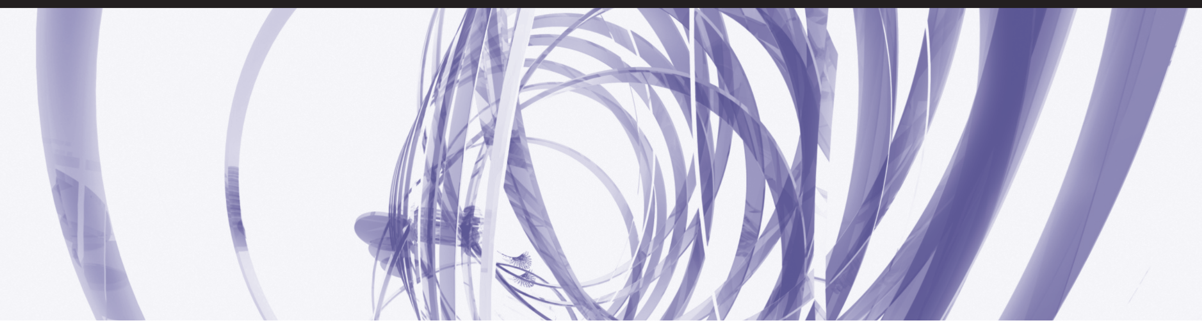
What is defined as a new market for market development purposes is complex. A new market may be closely related to the existing market and represent a related niche that the

organisation chose not to enter in its initial choice of market segments despite its attractiveness, for reasons such as financial constraints or lack of easy access. Alternatively the new market may be based on portraying the benefits or usage of the product in a new way to attract new user segments. This approach involves a degree of risk in that in repositioning the actual product to attract a new market segment, the original or core market segment may become disenfranchised. A third approach to market development which is commonly used is to expand geographically, either within the same country or internationally.

Depending on the type of market expansion planned, the strategic problems to solve will vary. Consistent within any market development strategy, however, is the need to systematically evaluate the new market in much the same way as a new product would be examined combined with the need to develop specific strategies to counter the inevitable reaction of competitors already operating in the market that the organisation is about to enter.

Growth strategy 3—Product development

CHAPTER 9



Introduction

Product development involves creating new products to meet the needs of existing markets. Product development is often perceived as similar in the level of risk to market development as in both cases the organisation is working with one familiar element of the marketing strategy. In the case of market development, the organisation's strength is in the perceived quality or value of its product whereas in the case of product development, the organisation's greater strength is in its knowledge of, and attractiveness to, the market. Organisations with strong brands tend to find product development an attractive strategy as it allows them to leverage off their reputation and further penetrate their existing customer base and increase purchases and loyalty by providing new product solutions. This chapter will include discussion of the assumptions of product development strategies and a detailed overview of the product development process.

Tactical value of product development

With the creation, delivery and communication of value lying at the core of the organisation's relationship with the customer in contemporary marketing theory and practice, product development can be seen as the opportunity to create a value offering that:

- replaces an existing value offering provided by the organisation
- replaces an existing value offering provided by a competitor
- meets a new need in an existing market with a new value offering
- meets a new need in a new market (diversification).

Although the fundamental principles of product development can be applied to diversification strategies, for the purpose of this discussion, the emphasis will remain on providing products to existing markets.

The tactical value of the product development growth strategy lies in its ability to expand the organisation's capacity to meet the needs either of the current markets, or new markets. Product development for an existing market can lead into other aspects of Ansoff's Growth Matrix. Having acquired new customers via a market development strategy for the new product, these customers can then be used as the basis for a market penetration strategy. Alternatively, having used the 'new' product to meet the needs of a current market, it can be also be leveraged into use as the basis for market development to enter new markets. Finally, organisational knowledge and experience gained from successfully implementing product development for existing markets can be used for the basis of a new product–new market diversification strategy.

Whilst product development has many rewards, the development of a new product involves considerable costs, including the possibility of the new value offering failing to capture the market. Creating new or modified alternatives to existing successful products may cannibalise the existing market and lead to static or declining profitability rather than create the growth in the customer base, and ultimately profitability, sought by the organisation. Forecasting costs, growth and market demand is difficult, and consequently new products are extremely vulnerable to sudden shifts in technology or consumer preferences destroying the market demand whilst the product moves through the new product development process.

Ansoff revisited: assumptions of the product development model

As with the other elements of Ansoff's Growth Matrix, the product development strategy needs to meet a series of preconditions for it to be applicable to the organisation as a business strategy. Product development, where the organisation finds a product to meet the needs of the market, can be seen as the mirror strategy to market development where the efforts are on finding a market for the existing product. At the same time, product development efforts are focused on a similar outcome of growing the organisation's share of a market which can then be targeted for a market penetration campaign. In order for the organisation to attempt a product development strategy, there are three preconditions that need to be met:

- an existing market
- customer retention
- an unmet need in the current market.

Product development does not occur in a strategic vacuum. New products can be derived from ideas that emerge during the design and implementation of market development or penetration strategies. This is particularly true where use innovation provides the impetus for creating a new product to meet an emerging need in the existing market.

Existing markets

Product development differs from diversification by one key element—the existence of a current market for the product offering. Diversification, in contrast, is based on the delivery of a new product to a new market. With the existence of a current market, there is also the implied assumption that this market either is serviced by a current product from the organisation, or has some other form of interaction with the organisation.

Customer retention

The second assumption underpinning product development as a growth strategy is that the organisation has a pre-existing customer base. The purpose of introducing a new product is either to grow or retain the existing customer base by better satisfying its needs with new product variations. With product development having a partial focus on customer retention, the issues raised in Whitwell, Lukas and Doyle's (2003) six keys to retaining customers will be applicable to the product development strategy.

Unmet needs

Whilst all aspects of growth-based strategy assume a level of unmet demand in a market, product development is based on the assumption that the market has a need for a different product than those currently available, or that the organisation can create a competitively superior alternative to the current products in the market. Given the heavy dependence on unmet needs for the success of the strategy, organisations rely heavily on two major factors: the internal analysis of core customer outcomes (Chapter 4) to identify unmet needs with existing customers, and external market research with particular emphasis on industry analysis, competitor analysis and market segmentation (Chapter 6).

Core principles of product development-based growth

One of the linguistic biases of the strategy literature is the assumption that 'new' equates with 'will provide benefit to the customer'. The product development literature is prone to this bias, and is particularly strong where the phrase 'product development' is seen as interchangeable with 'new product'. The range of alternative methods for developing a value offering that matches the needs of the market is wider in product development than in new product development. Proctor (2000) outlines a range of value offerings that can be created through product development. These are:

- *new to the world*, where the value offering to the market is a completely new product, service or idea which requires the customer to adopt a new form of behaviour (discontinuous innovation)

- *new category entries*, where the product is new to the organisation, but may be an older product in the marketplace
- *product line extensions*, where the organisation offers a derivative form of the product with a new feature set that does not significantly change the product functionality or value offering
- *product improvements*, where the organisation releases a product upgrade, or enhances the performance of a product
- *repositioning*, where an existing product is repackaged, rebranded or reintroduced to a market to occupy a new market position, or to deliver a new set of solutions to an existing market problem. Repositioning can also be used to present use innovations to the market where the focus of the organisation shifts from the original intention for the product to delivering the value solution created by the use innovation.

Wood (2004) identifies three successful areas that the organisation can draw on to develop the products for existing markets:

- *need identification*, which is where the organisation looks to the market to determine what unmet needs are present
- *solution identification*, where the organisation looks for market demand for a set of solutions which they use as the basis for creating a new product to provide that solution. This tends to be a business-to-business and supplier–consumer style of product development. For example, the organisation may be aware that its customers have to assemble a range of component parts for use in their products. Developing a new integrated product to replace the assembly process is an example of solution identification product development
- *market research*, which is where the product development process arises from information gathered in the internal (Chapter 4) and external (Chapter 5) analysis. Products developed as a result of analysis of the competitor environment and competitor signals would come under this category.

In addition, the product development process can emerge from within the organisation through:

- *employee innovations*, which is where the staff create a new product as part of their employment or where they identify an opportunity in the market from their own creativity
- *listening post-based innovations*, which is where the front line sales and counter staff identify an unmet market need or solution, and report this back to the organisation. This approach relies heavily on the existence of a knowledge management system that enables the data gathered at the customer-interaction level to flow through the organisation
- *supplier-driven innovation*, which is where the organisation gains an innovative concept from its suppliers upgrading component products, or through use-innovation suggestion from the supply chain.

Issues in product development: is the product new to the market or the organisation?

Successful product development is heavily dependent on the ability of the organisation to view the product from the perspective of the market, and to adjust where necessary. Product development emphasises the creation of products that are new to the organisation to deliver to existing markets. Consequently, those markets which have been targeted may already have an existing product or solution. The 'new' innovation from the organisation's perspective therefore may be an 'old' product to the consumers.

Types of innovations

In brief review, there are three overall types of innovation:

- *really new products (discontinuous innovations)*, which are those types of new products that need the consumer to form new behaviours
- *quite new products (dynamically continuous innovations)*, which are those types of products that represent a radical shift or upgrade in a product category but which can be traced to an existing product, behaviour or concept
- *continuing products (continuous innovations)*, which are those products with only minor changes in the product.

Using a product development strategy requires the organisation to understand the perception of both the organisation and the market towards the product. Table 9.1 outlines a grid approach to identifying potential differences in perception.

TABLE 9.1 Market and organisation perception of the product

		External view to new market		
		Continuous (same product)	Dynamic (improved product)	Discontinuous (new product)
Internal organisational view of the product	Continuous (current product)	Market penetration/ Market development	Market development	Market development
	Dynamic (modified product)	Market development	Product improvements	Repositioning
	Discontinuous (new product)	New category entry	Product line extensions	New to the world/ Diversification

The categories of relevance to product development strategy are:

- *dynamic–continuous*, which is the situation where the organisation offers a heavily modified version of its existing product to the market which is perceived by the market to be the same, or similar, to current products on offer. This is an indication that the organisation has not invested sufficient attention to the competitor analysis, and has failed to deliver a competitive advantage despite the modifications to the product.
- *dynamic–dynamic*, which, whilst strictly speaking part of the market development strategy, may be a borderline case for new product development depending entirely on the level of modification done to the original value offering. Use innovations may be presented as original and 'new' products in their own right, or as a product line extension. Product line extensions that convert powdered products to liquid or vice versa are examples of dynamic–dynamic product developments.
- *dynamic–discontinuous*, which is where the modification of an existing product either through repositioning or use innovation has effectively relaunched the product as a new solution in the market.
- *discontinuous–continuous*, which is where the product is new to the organisation but is an 'old' value offering to the marketplace. This is usually the domain of the new category entries where an organisation extends its operations into a new series of products that tap into an existing market. Although the temptation is to sell the product as 'new', it should be positioned on competitive advantage or the brand strength of the organisation, rather than the 'newness' of the product.
- *discontinuous–dynamic*, which is where the product is technically new to the organisation but only represents a change in how the solution is provided to the market. This occurs when the organisation brings a new category entry to the market with a clear competitive advantage over the existing products and solutions.
- *discontinuous–discontinuous*, which is the 'new to the world' product that neither the market nor the organisation has seen previously. New to the world products can also be the basis for diversification strategies. In the product development context it represents the organisation addressing a market need with a totally new solution, rather than an incremental adjustment of existing products.

The remaining positions not discussed in Chapter 9 are based on the assumption that the product being offered by the firm is not new to the organisation (or at least significantly modified), since offering an existing product to an existing market is market penetration and offering existing products to a new market is market development.

Model of new product development

In Chapter 8, the new product development model was modified to address issues associated with the development and targeting of a new market segment. Consequently,

there will be a degree of overlap and repetition. The new product development model consists of ten component steps:

- *corporate strategy*, which is the objective of the organisation in aiming for new product development, and a clarification of the limits imposed by the organisation's overall goals.
- *product ideas and the idea generation process*, which is the phase where product concepts, value offerings and new solutions for existing market problems are generated via market research, customer feedback or any of the sources discussed previously.
- *exploration, analysis and product screening phase*, which is where product ideas are first critically examined to determine if they have sufficient merit or represent a good enough fit with the overall strategic direction of the firm to be further developed.
- *concept testing*, which is where the surviving ideas are examined in terms of what benefits they offer the market and how they can be positioned to meet the needs of the target market.
- *business analysis*, which is where the financial analysis of the costs and benefits of developing the concept into a full-blown product are examined.
- *brand development*, which is the stage of the process dedicated to the development and testing of the marketing messages that will be used to communicate the value offering to the public.
- *implementation/product development*, which is where the new product is developed from a prototype to the final offering to be delivered to the consumer.
- *test marketing*, which involves releasing the product into a smaller market segment to assess how it performs under open market conditions.
- *launch/commercialisation*, which is where the final product offering is commercialised and released into the target market based on the marketing plans developed for the product (Chapter 14).
- *control*, which is where the organisation uses marketing metrics (Chapter 15) to assess the success or failure of the new product.

Table 9.2 overviews the steps of the new product development and the stakeholders most likely to be involved in those processes.

This table is a summary of the likely interactions between a product concept and the organisation's stakeholders. Although each stakeholder can have an influence at any stage of the process, key interactions between stakeholders and the new product development are highlighted in the relevant sections below.

When applying this model it is important to remember that all models are an abstraction of reality. Whilst each of the steps outlined above occurs during the process of new product development, they do not necessarily occur in a sequential manner. In practice different steps may be undertaken simultaneously, for example financial analysis and brand development. Further, new product development tends to be a multifunctional and iterative

TABLE 9.2 Steps, stakeholders and supporting authors

Component	Stakeholders	Supporting authors
Corporate strategy	Board of Directors Managers Shareholders	Doyle (2002)
Ideas and idea generation	Social pressure lobby groups Society/citizens/community Employees Distributors	Doyle (2002) McDonald (2002)
Exploration and analysis/ screening	Employees Managers Suppliers	Doyle (2002) McDonald (2002)
Concept testing	Customers Competitors Social pressure lobby groups Employees Suppliers	Doyle (2002) McDonald (2002)
Business analysis	Board of Directors Creditors and financiers Distributors Employees Managers	Doyle (2002) McDonald (2002)
Brand development	Employees Managers	Doyle (2002)
Implementation/ product development	Employees Distributors Managers Suppliers	Doyle (2002) McDonald (2002)
Test marketing	Customers Local community Distributors Employees Suppliers	Doyle (2002) McDonald (2002)
Launch/commercialisation	Customers Local community Media Social pressure lobby groups Distributors Employees Managers Suppliers	Doyle (2002) McDonald (2002)

Control	Board of Directors Local community Media Managers Shareholders Government Unions	Doyle (2002)

process whereby representatives of different aspects of the organisation such as finance, manufacturing, marketing and logistics all have an input into the process. The analyses undertaken at later stages of the process are influenced by a combination of these interactions plus the analyses undertaken at earlier stages. It is not unusual to reach a point in the process where a blockage is encountered which necessitates one or more steps backwards through the model to reanalyse earlier stages of the process.

Corporate strategy

The first step in the product development process involves outlining the organisation's objectives in developing a new or revised value offering (Doyle 2002). This stage is vital for shaping the overall direction of the process, as product development should be considered as part of a planned process of growth. The corporate strategy section defines the scope of the product development operations and the purpose of the product development, and assists the organisation in priority setting. Corporate strategy provides the framework for product development within the organisation and is based on aligning the creation of new value offerings with the following elements:

- *corporate purpose*, which is where the product development strategy matches the overall organisational purpose. For example, developing a high-status, high-cost, technologically complex industrial strength coffee machine is inconsistent with the organisational purpose of a firm with a corporate purpose of mass production of affordable kitchen products. Where an organisation decides to develop products that radically move away from its current purpose, it will be a diversification strategy, rather than product development.
- *capability profile*, which is the ability of the organisation to actually produce a final product. Whilst idea generation is usually recommended to be as unrestricted as possible, understanding the capabilities of the organisation will assist in focusing on what value offerings can realistically be offered. In addition, new or revised product offerings can often be developed from focusing on adapting the current capabilities of the organisation (continuous or dynamic products) rather than developing new products that also require new capabilities (discontinuous). Capability profiles are used again in the product development process during the exploration, analysis and filtering steps.

- *growth direction*, which is an understanding of the overall plans of the organisation to grow, and whether the organisation is going to be willing to commit resources to product development-based growth ahead of market development or market penetration.
- *organisational objectives,* which are those objectives outlined in Chapter 6. Focusing on what the organisation is attempting to achieve can provide a framework for exploring new or modified value offerings.

As product development is based on serving an existing market, it should make use of the organisation's plans for that market together with the organisation's broader market objectives as a framework for exploring new ideas. If the organisation has a strategic goal of being the market leader, then ideas can be targeted towards innovation, new concepts and competitive advantage. Similarly, if the overall principle of the organisation is to be a market follower, and to produce 'me-too' products for its markets, then idea generation can be focused on creating improvements to existing market solutions. This phase also brings the stakeholder needs of the organisation to the fore—that is, the needs of the board of directors, managers and shareholders.

A clear view of the organisation's objectives and the needs of the stakeholders will help maintain a focus on the prime areas for product development, which in turn assists the organisation's growth strategy. For example, if the shareholder stakeholders have expressed concern regarding the organisation's propensity to engage in too many 'high-risk' ventures, then the optimum product development strategy that satisfies the needs of the organisation and the stakeholders will involve adapting current products (continuous) or copying competitor products (dynamic), rather than developing entirely new products (discontinuous).

Ideas and idea generation

Idea generation is complicated, and is stimulated by a wide variety of factors. There are ten broad sources where ideas from new products can be acquired, generated or otherwise provided to the organisation. These are:

- *acquisition of ideas from third-party sources*, where the organisation purchases a new product concept from an external source (Doyle 2002, Viljoen & Dann 2003). Third-party sources can include research and development laboratories, smaller competitors and start-up organisations or product development consultants.
- *competitor imitation*, where the organisation copies an existing product or value offering from its competitors for the purpose of imitation or product improvement (Doyle 2002; Viljoen & Dann 2003). Although the provider of the original product solution may have the first mover advantage, me-too products can often provide a competitive advantage for the second-to-market organisation. In particular, second-to-market organisations have the advantage of being able to work with existing market demand created by the market leader and learn from any mistakes made by the leader.

- *creativity*, which is the nebulously defined concept that underpins the entire new product development process (Doyle 2002; Hooley, Saunders & Piercy 2004, Viljoen & Dann 2003; McDonald 2002). Creativity is more likely to occur in a supportive workplace environment that allows employees and management the freedom to question if the current method of meeting customer needs is the optimum process, and the framework to propose alternative approaches.
- *customers*, which is where the organisation's customers suggest alternative product solutions that would satisfy their currently unmet needs (Doyle 2002). Ideas generated from customers can also arise from market research (Chapter 5), and customer satisfaction benchmarks in the core customer outcomes measures (Chapter 4). Ideas from customers are restricted to customer suggestions of new products or new solutions that they need from the organisation.
- *distributors*, where the product distributors act as a listening post for the organisation and suggest value offerings that would meet their needs, and the perceived needs of their main market (Doyle 2002). For example, a distributor may suggest packaging innovations, different product sizes or a different version of the product for each of the markets that they service.
- *internal innovation from employees*, where the employees of the organisation develop new versions of the product, or improve on the value offering through their experience with the product (Doyle 2002; Viljoen & Dann 2003). Whilst this is related to creativity, it also represents the level of involvement and ownership the employees have over the product and the production process of the value offering. For example, in a highly controlled and scripted service environment, the employee is unlikely to consider suggesting a product innovation. In contrast, highly customised service encounters that allow for a degree of freedom based on the skills of the employees will often lead to internal innovations that can be identified, refined and reoffered as new products to the market.
- *market centric management*, which is where the management of the organisation examines the needs of the market and the satisfaction level of current customers against the framework of 'What else can the organisation do to satisfy the customer?' (Viljoen & Dann 2003).
- *research and development*, where a dedicated component of the organisation is focused on developing new products, finding new uses for existing products, and enhancing the value offering of the firm (Doyle 2002). Idea generation from research and development is tied closely to overall organisation goals—for example, 3M has an organisational objective of a fixed percentage of its annual revenue coming from 'new' products.
- *suppliers*, where product innovations are suggested by the providers of the component parts of the organisation's current value offering. Supplier-driven innovations are also likely to be part of just-in-time manufacturing relationships, and the longer-term relationship marketing objectives of the supplier. From the supplier's perspective, assisting their customers with product innovations

represents a possibility of continuing the relationship, and either engaging in product development or product development growth in the supplier's organisation.

- *use innovations*, where the organisation capitalises on the creativity of the marketplace in how existing customers have adapted the organisation's product for a new value offering. If the organisation does not create a new product tailored for the value solution offered by the use innovations, then it remains a market development strategy.

Lead user analysis as idea generation

Lead user analysis was outlined in Chapter 6 as part of the external marketing analysis of the customer. In the external analysis, this was a four-step process based on Best's (2005) model, which was:

- Step 1: Identify lead users who have extended the use of the product
- Step 2: Study how lead users have extended the product usage
- Step 3: Discover how products could be modified to improve usage
- Step 4: Develop a more complete customer solution or new product.

Lead user analysis can also be used to capture use innovations in the marketplace. This gives the organisation an opportunity to develop a product specifically tailored to the use innovation which can then be on sold to the existing market (new product, current market), or which can be used for market development.

Customer retention as idea development

Viljoen and Dann (2003) proposed a managerial level process of idea generation based on the notion of 'market centring' which is where the organisation constantly reviews its market position and value offering against the framework of 'What else can we provide to our clients?'. In Chapter 7, six keys to customer retention were outlined, based on Whitwell, Lukas and Doyle's (2003) checklist. These elements were:

1. Select and prioritise customers
2. Customise the value proposition
3. Enhance value
4. Monitor satisfaction and loyalty
5. Follow up on complaints
6. Build customer partnerships.

Steps 2 and 3 of the Whitwell, Lukas and Doyle framework can be used as part of the idea generation process for providing new or modified products based on the Viljoen and Dann (2003) market centring concept. By constantly reviewing what value proposition is being offered to the client, and what else can be provided to meet market needs or enhance value, the organisation can use this review process as a source of new ideas for product development.

Exploration, analysis and screening

The idea exploration, analysis and screening phase is conceptually similar to the evaluation and selection phase of the market segmentation process. The overall objective of this step of the product development process is to deliver a series of viable product offerings that can be developed for concept testing and business analysis by filtering out those ideas that should be rejected and then concentrating on those that should be progressed.

There are three filtering processes to consider for the exploration phase. These are:

- base level filtering
- corporate fit
- capability profile filter.

Base level filtering

Having created a range of product concepts from internal and external sources, the next step of the process is to filter through the pool of ideas for the good, bad and 'needs work' concepts (Hooley, Saunders & Piercy 2004). In this context, ideas are:

- *good*, where the idea has a basic level of merit that warrants further examination and analysis
- *bad*, where the idea has an immediate conflict with the organisational goals, current market or has some overt or irreconcilable flaw
- *needs work*, where the idea can be developed in the future, or where the product concept is not sufficiently refined to allow it to be accepted or rejected for further analysis. These types of ideas should be sent back for further work rather than being discarded.

This preliminary analysis is based on the subjective opinions of the management and employees responsible for the product development process. In the context of product development, an idea marked as 'good' indicates it passes first inspection for analysis under the rest of the filters. Similarly, if the 'good' ideas fail to come to fruition, the 'bad' ideas are put through the filter next, before returning to the 'needs work' category. This is a prioritisation phase rather than an elimination step.

Corporate fit

Testing an idea for its corporate fit is a filtration method based on establishing if the idea is consistent with the rest of the organisational activities and goals (Doyle 2002) There are four measures for assessing corporate fit:

- *consistency with corporate purpose*, which is the match between the idea and the corporate purpose outlined in the first step of the new product development process. This may give the product development process an inherently conservative bias by constraining new product concepts to the existing organisational purposes. However, if the corporate purpose includes 'innovation' as a central concept, this step should be used to prioritise new product solutions since that will match the corporation's stated objectives.

- *consistency with objectives*, which is the extent to which the product concept will meet the organisation's objectives (Chapter 6) and growth strategies (Chapter 9). This differs in focus from corporate purpose in that this step asks the question 'Does this product concept help us meet our objective?' rather than corporate purpose question 'Is this compatible with our organisation?'
- *fit to goals for the product line*, which is the related sub-question of whether the idea fits within the objectives and goals for the product line (e.g. quality improvement). The question being asked by this stage is whether the idea matches the rest of the plans and objectives for the existing product lines. For example, if the organisation has determined through the Directional Policy Matrix (Chapter 2) that it should engage in a withdrawal from a market, product concepts designed to meet the market the organisation is leaving should be rejected irrespective of the implicit quality of the product concept.
- *fit to goals for the market*, which is the extent to which the product concept will actually meet the organisation's plan for the market in terms of servicing the market's needs. For example, if the organisation is aiming to develop new products to meet a specific market need, ideas that are not going to service this need would be rejected, or set aside for separate review.

Capability profile filter

The third filter process is to assess the idea against organisational capacity. This involves assessing the extent to which the idea represents a continuous, dynamically continuous or discontinuous innovation within the organisation. Essentially, the idea is assessed against the ability of the organisation to actually produce the final product. Typical criteria used in such an assessment are outlined by Doyle (2002). These are:

- *production*, which represents the match between the organisation's production capacities (including employee skills, available equipment and current production processes) and those required by the new product concept. If the product requires new production facilities, this will require major capital investments and organisational restructuring.
- *technical*, which is the extent to which the adoption of the product concept relies on existing technical capacities within the firm, or will require the organisation to adopt new technologies in order to deliver the product.
- *marketing*, which is the extent to which the product concept fits into the current marketing program. This filter step examines whether the current marketing strategies and the marketing department could effectively communicate the value offering to the market, and if not what changes would be required for this to be possible.
- *distribution*, which is the capacity of the organisation to deliver the value offering to the market. Introducing a brand new product will require the organisation to work with its existing distribution stakeholders to ensure the new product can be delivered to the market. Alternatively, if the new product (e.g. digital music) will

introduce a new type of distribution (online downloads) versus the current method (physical CDs in music stores), this will impact on the organisation's relationship with its suppliers.

- *finance*, which is the level of additional investment that will be required for the new product concept to be brought to the market. This includes the available money within the organisation and the likely willingness of the financier and creditor stakeholders to support the product being developed.
- *people*, which is the match between the human resource needs of the product concept and the current employees. Introducing a product with a radical shift from the current technical capacities may require recruitment of new skilled employees, the displacement of current staff without the requisite skills (job losses) or major investment in retraining and up-skilling.
- *stakeholders*, which is the extent to which the product concept matches the needs of the organisation's key stakeholders such as the shareholders, and the standards of the broader community stakeholder. This includes the potential environmental impact of the product concept in terms of resource consumption, capacity to be recycled or to use recyclable materials and related environmental issues.

The end result of this filter step is an understanding of the capacity of the organisation to deliver the product concept at the present time, and what levels of internal change and development would be expected in order to create, communicate and deliver the value offering being proposed.

Concept development and testing

Concept development is where the product ideas that have survived the initial filtering process are developed into full value offerings which are tested against the needs of the market. The process of product development can be vulnerable to focusing on the features of the service or product, rather than the value solution being provided to the customer. The purpose of the concept development and testing phases is to ensure that the organisation offers a solution to the consumer need or want, rather than a set of features. Similarly, the positioning of a product concept is, at this stage, more important than the technical specifications or physical features. Where the concept is based on an existing product, either in a new market or as a dynamically continuous innovation, concept testing can draw on the value proposition analysis (Chapter 4) and customer analysis (Chapter 5). Where the organisation is developing a new product, direct market research with potential customer groups is required. In both instances, Doyle (2002) identified the six criteria to use to assess the strength of the product concept:

- *communicability*, which is the extent to which the test market can understand the idea behind the product concept
- *believability*, which is the level of trust the customer has in the ability of the product to deliver the outcomes promised by the organisation
- *need*, which is the extent of the demand for the solution being offered by the product

- *need gap*, which is the extent to which the demand for the solution is already being satisfied by other products in the market
- *perceived value*, which is whether the consumer believes the product is worth the price being proposed by the organisation
- *usage*, which is the amount of use the customer would get from the product, and what, if any, initial use innovations can be identified in how the customer would use the product concept.

For a product being developed for an existing market, the most vital emphasis is on the needs gap and perceived value. If there is no needs gap, and the market is satisfied with the current offerings, then the organisation either has to create a needs gap by displaying a relevant competitive advantage for the customer, or forgo the creation of the new product offering.

Business analysis

Business analysis is the first stage of the process to examine the financial implications involved in the creation, communication and delivery of the new value offering. It involves a combination of the following:

- projected costs of developing the product (financial analysis)
- projected costs of delivering the product to the market (financial analysis)
- expected revenue from the value offering, including the potential for additional market penetration and market development strategies (financial analysis)
- the attractiveness of the market for the firm (demand analysis)
- the attractiveness of the product for the market (demand analysis).

Business analysis makes use of a series of the planning models from Chapters 2, 4 and 5. In particular, the Directional Policy Matrix (Chapter 2), financial analysis (Chapter 4), Porter's Value Chain (Chapter 4), market attractiveness analysis (Chapter 5), competition analysis (Chapter 5) and business environment analysis (Chapter 5) should be reviewed.

Financial analysis

The financial analysis aspects of the business analysis tie into the balanced scorecard (Chapter 4) internal analysis, along with the financial objectives of the organisation (Chapter 6) and the interests of the shareholder stakeholders (Chapter 3). Viljoen and Dann (2003) outline three broad areas for consideration in analysising the financial potential of a product concept. These are:

- *break-even analysis*, which is the estimated revenue from sales required to cover the costs of the product development process and the initial product launch (including the marketing costs of developing the market, creating awareness and driving demand for the product).
- *payback period*, which is the length of time it will take for the organisation to reap a benefit from the investment in the product. Shorter payback periods are

obviously preferred for cash flow reasons, and to reduce vulnerability to shifts in the market and attacks from competitors.

- *return on investment (ROI)*, which is the percentage the organisation will earn from the investment in the new product. Higher ROI indicates lower initial costs and high levels of expected profit and sales.

Demand potential

The second aspect of the business analysis capitalises on the knowledge generated in the internal and external analysis conducted previously, and repeating key analysis areas for the purpose of assessing the value of the product concept (Doyle 2002). Demand potential uses the conceptual framework of the Directional Policy Matrix by assessing the strength of the organisation (exhibited through the product concept) and the attractiveness of the market (based on the level of demand for the product concept). Within this broader framework are specific areas that need to be addressed. These are:

- *customer demand*, which is based on both the customer analysis (Chapter 5) and market segmentation (Chapter 6). Where the product concept is based on an existing product, the value proposition analysis (Chapter 4) and the core customer outcomes measures (Chapter 4) should be used. Measures of demand examine whether the market is sufficiently viable to warrant the investment of the resources in the new product, and whether investing in this initial market can be a starting point for market penetration or market development.
- *market size*, which is an estimation of the total volume of the market segment base (Chapter 6), size of the overall market and information on the size of the overall industry which is derived from the industry analysis (Chapter 5). It is also possible to use measures such as the Share Development Index developed by Best (2005) which was overviewed in Chapter 7 as part of the market penetration strategy. In new product development, the Share Development Index would be used to determine if the new product could be used to acquire market share.
- *market growth*, which is the projected rate of growth or decline in the market over a period of time. This measure is useful in determining if it is worth investing in an underdeveloped market which has strong growth potential, or whether to abandon plans for a currently promising market which is projected to experience negative growth in the near future.
- *socio-political risk*, which is the likelihood of negative reactions from the key stakeholders of government and the broader society. The introduction of a new product can create socio-political upheaval, and can result in government intervention to introduce restrictions on trading and control over production quality. For example, a new drug introduced to treat a common ailment is subjected to a wide range of government interventions to ensure consumer safety.

Brand development

The brand development phase occurs in parallel with the product development and implementation phase as the organisation creates the initial product offering to the public, and develops the marketing messages that will be used to communicate the new value offering. This is where the marketing mix is first introduced into the product development process, as the organisation will have a better grasp of the costs of the product relevant to price setting, and the features of the product following the detailed concept testing in earlier phases of the process. The brand development phase focuses on micro-level value offering issues identified by Doyle (2002). These include:

- *product tests*, which involve the testing of the physical product for a range of factors such as durability, safety, performance and ability to meet the needs of the consumer.
- *packaging test*, which includes examining the appropriate packaging sizes for different products. This phase also involves working with the distributor stakeholders and retailers to ensure that the packaging being proposed by the organisation will fit into the retailer shelf space and can be processed through the current distribution system.
- *name test*, which involves market testing potential product names. Until this stage of the process, most products have place-holder names or project identifiers. Occasionally these names become the final product name, particularly in the pharmaceutical industry, although most products are given names as part of the branding and positioning strategy, rather than the internal R&D processes.
- *price research*, which is a combination of the economics of the financial elements of the business analysis setting the minimum price levels required for profitability, break-even and the organisation's preferred return on investment, with the psychology of pricing based on brand and product position. Yes, it is that complex.
- *advertising tests*, which is where the communication of the value offering is test-marketed to ensure two outcomes. First, that the organisation is communicating the value offering clearly to the market and second, that the market is interpreting the offering and advertising in an appropriate manner. This also ties back to the communicability aspect of the concept testing phase.

Brand development involves the creation of strategic and tactical marketing plans, along with the relevant promotional plans, positioning strategies and communications strategies. This is further investigated in Chapters 14 and 15.

Product development

The product development phase is where the value offering that has been tested, analysed, refined and costed is given final approval for development. Product development is described by Viljoen and Dann (2003) as a cyclical process of development and testing which moves through product concepts, prototypes and market testing until a final market ready product is produced. Hooley, Saunders and Piercy (2004) emphasise the need for the

product to provide an advantage to the consumer, which must take the form of delivering greater value than that offered by the competitor's products. In addition, Hooley, Saunders and Piercy outline reasons why products which have passed the complex internal product development process may still fail in the open market. These include:

- *no demand*, which means that despite the market research and market testing conducted in the previous phases, the consumer still does not want the final product offering from the organisation.
- *competitors*, which is where the product is counter-matched by the organisation's competitors who produce a product that offers better value to the consumer.
- *product failure*, where the product fails to meet the needs of the market, or simply does not work as promised. For example, certain brands of laptops were prone to failure due to a flaw in the LCD construction process by the manufacturer's suppliers.
- *price barriers*, where the cost of adopting the product is too high for the market. One overlooked facet of pricing for many products is the total cost of the product once shipping is included. This is a factor that can reduce market demand for those international and online products which are competing against domestically available alternatives.

Test marketing

The final phase before launching a new product into the core target market is test marketing, in which the organisation releases the new product to a targeted sub-segment of the desired market. Test marketing is designed to allow the organisation to field test its marketing and product design with consumers under real market conditions. Given the costs and risks involved in going public with a new offering, not all organisations will implement this phase. Alternatively, firms are increasingly using computerised simulations to predict probable success in the market and are bypassing this phase altogether.

Should the organisation decide to take this step there three issues that need to be addressed:

- the market chosen as a test market should be sufficiently restricted to prevent contamination of the major market should the product fail
- the test market must be sufficiently representative of the final market to avoid false positive and false negative results
- releasing the product into the market in a test market will allow competitors to access the product, and potentially develop their own versions.

One risk inherent in testing is that competitors may choose to modify the market conditions in the test market region by offering product promotions, sales discounts or other incentives to block the new product from selling.

Launch/commercialisation/implementation

The penultimate stage of the product development process is the actual release of the new product into the target market segment. Although this is the ultimate outcome and goal of the

product development process, it is also the shortest section of the chapter. Once the product has been cleared for launch into the market, this process is then covered by the marketing practice of communicating and delivering value to the customer. The launch, commercialisation and implementation phase is covered in more depth in Chapters 14 and 15.

Control

The final step in the product development process is to engage in the control and review stage, as advocated by Doyle (2002), Viljoen and Dann (2003), Shaw and Merrick (2005) and Kotler and Keller (2006). The control phase involves the implementation of marketing metrics such as retail audits, consumer panels or sales figures. Marketing metrics and control are examined in detail in Chapter 15.

Competition and product development

Product development is one of the most aggressive methods of engaging the organisation's competitors. Developing a new product for an existing market usually involves identifying a desirable market segment being serviced by a rival organisation, and preparing a product that will be superior to the competition. This type of approach will involve head-to-head conflict between the organisation and its products, and the offerings of the rivals in the market. Similarly, developing a new product for an existing or new market may encourage rival organisations to copy that value offering and target the same markets. Table 9.3 outlines the most common competition strategies.

TABLE 9.3 Competition, strategy and tactics for new product development

Technique	Tactic	Offence	Defence
New to the world	Frontal attack Flanking Encircling	New value offering New method of meeting the market needs Exclusive distribution channel	'Me-too' product Repositioning existing value offering to compete directly against the new product
New category entries	Frontal attack Flanking Guerrilla	Competitive advantage Differentiation strategy (Chapter 11) Cost advantage (Chapter 10)	Repositioning Relationship marketing Pricing Exclusive distribution deals that reduce the available market channels

Technique	Tactic	Offence	Defence
Product line extensions	Flanking Bypass Guerrilla	Competitive advantage Alternative delivery of a current offering	Imitate alternative value distribution technique 'Me-too product' Introduce product improvements to existing offering to counter the line extension
Product improvements	Frontal attack Flanking Bypass Guerrilla Non-confrontational	Differentiation Increased feature set Increased functionality	Determine if the new features are meeting market needs more effectively than current product offerings and counter with improved product offerings as necessary
Repositioning	Frontal attack Flanking Bypass	Alter the perceived use of the product Alter the perceived competition by position against new competitors	Counter with reinforced branding, integrated marketing communications (IMC) and relationship marketing

Conclusion

Innovation and new product development are advocated by marketing strategists as essential for the ongoing relevance and survival of the organisation. Although new products may be perceived as the lifeblood of the organisation, the process of creating and developing relevant new value offerings is complex, expensive and risky.

New product development as discussed here is based on the assumption that the organisation is creating new product variations to satisfy the needs of an existing market. Consequently the firm is assumed to have a good understanding of the characteristics, dynamics and needs of its customer segment and is most likely to derive a number of new product ideas from existing customers and other stakeholders.

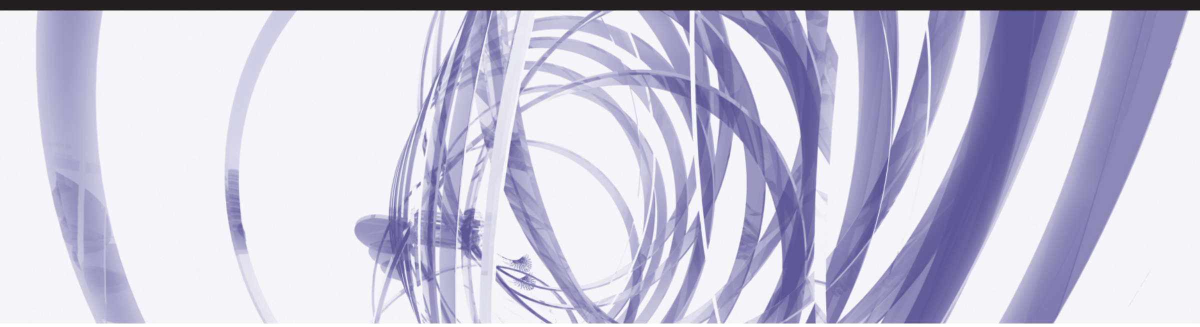
As is the case with all growth strategies, the extent to which product development is integral to the organisation's operations is guided by overall corporate objectives and the

capacity of the firm to support the product development process. In this text the traditional model and stages of the product development process are outlined in detail. Although the steps are presented sequentially for the purpose of explanation it is important to realise that in practice the process is iterative and new product development teams will often return to an earlier stage of analysis to refine or clarify the developments of a later stage.

New product development is also guided by the nature of the market and the competition. Innovations and new product offerings are more important in markets such as those dealing with technology where there is an expectation of new software upgrades on an annual basis than in more stable industries such as furniture design. Similarly in highly competitive markets such as fast moving consumer goods, minor variations to product lines are common. Regardless of whether the extent of investment required or disruption encountered in the new product development process is minor or major, the value of new product offerings is determined by the extent to which they meet a genuine perceived need in the market.

Value addition and strategic competitive advantage 1—Cost leader

CHAPTER 10



Introduction

Cost leadership is one of Porter's (1980) Generic Competitive Strategies and concentrates on developing methods of obtaining the lowest production costs within market or industry segments. While cost leadership can lead to the lowest priced products in the market, being the cost leader does not oblige the organisation to offer low prices. Rather it can be used as a strategy which maximises both profits and the ability of the organisation to withstand short-term price-based competition, or can be used as the basis to block new market entrants. This chapter explores the cost drivers which can be influenced to create cost leadership, and the role of cost reduction on other aspects of the business strategy (such as pricing and positioning). It also focuses on the balance between cost reduction strategies and the need to continue to create, communicate and deliver value to the consumer.

Cost leadership as a competitive advantage

Cost advantage was outlined in Chapter 5 as part of the competitive position analysis. Cost advantage is the financial element of the process where advantage is derived from

producing the value offering at a lower cost than the competitor, thus providing more revenue per unit for the same market price. In this manner, it was defined as consisting of three component elements:

- *variable costs*, comprising the manufacturing, transport and transaction costs involved in the creation of the value offering
- *marketing expenses*, which are costs incurred in the acquisition or retention of the customer
- *operating expenses*, which are the costs associated with the continued operation of the organisation.

These three elements recur throughout the chapter as parts of different models of cost leadership.

Tactical value of cost leadership

Cost leadership is the strategic decision to compete by providing products at the lowest cost, but not necessarily the lowest price, in order to create a sustainable competitive advantage. The first and dominant drive of the cost leadership strategy is the financial objectives of the organisation. Creating an economic advantage through cost leadership provides the organisation with two forms of immediate shareholder value.

First, reduced costs can translate into increased profit per unit. Higher profit margins in turn lead to greater returns for the shareholders. Second, producing the same product for less cost than competitors allows the organisation greater flexibility in determining its prices. It also provides a buffer and gives the organisation the opportunity to decrease prices whilst maintaining relatively high per-unit profits when compared to the competitors. Reduced prices coupled with desirable products should lead to increased market share, improved economic performance of the organisation, and consequently improved shareholder value. However, shareholder value is not the sole determinant of the value of the cost leadership strategy. Proctor (2000) argues that cost alone is only one half of a competitive advantage. The organisation also needs to create cost efficiencies and provide a superior value offering to the market (Chapter 11).

Cost advantages are often developed by focusing on the core competencies of the organisation to maximise the efficient use of the organisation's resources (Chapter 4). Emphasising core competencies also assists other aspects of the organisation's business planning such as implementing a market penetration strategy. Combining improved cost efficiency with increased sales to the core customer basis should result in increased profits and shareholder benefit. Cost advantages on existing products also allow the organisation some leeway to cross-fund other projects through its product development and market development phases (Chapter 8 and 9). For example, an organisation may elect to use a cost leader strategy to increase the cash flow available to counter an unbalanced future-focused portfolio (Chapter 4). In this instance, the costs incurred in developing future products can be offset by focusing on cost leadership within the current products. In this

approach, the firm maintains current pricing levels, attempts to reduce costs in the current value chain, and offsets the research and development budget with these savings.

Cost leadership versus lowest price

The most common misunderstanding of the cost leadership strategy is the assumption that low production costs put the organisation under an obligation to set low prices for the consumer. There is no obligation, financial, commercial or otherwise for an organisation which has the cost leadership in the market to reduce its prices simply because they have achieved internal efficiencies. Whilst cost leadership can be used for reducing price to increase market share, it can equally be used to maintain prices and increase per-unit profit margins.

Further, cost leadership needs to be considered carefully against the rest of the organisation's positioning strategy, and the value offering delivered to the market. For example, luxury goods which are built around a series of social messages derived from the high cost of the product (and the implied scarcity of raw materials) can be harmed by cost leadership strategies which reduce price (altering the social message of exclusivity) and by the reduction in perceived product quality which can result from the lower price.

Risks of cost leadership

As with all forms of strategy, there are risks inherent in adopting a cost leadership approach. Focusing on costs and reduction of costs by the elimination of organisational functions (such as service delivery, research or marketing) can create organisational vulnerabilities. For example, Whitwell, Lukas and Doyle (2003) illustrate that organisations that attempt to cut costs by ceasing product development increase their vulnerability to rapid technology change. Similarly, reducing costs by decreasing market research (Chapter 5) can result in the organisation being unaware when the needs of the key target markets shift. Financial gains derived from lowering costs will not replace lost customers if the market changes and the value offering becomes irrelevant to the organisation's core target markets. Similar risks arise from any attempts to reduce costs at an organisational level by reducing spending on secondary components of the value chain. Whilst individual products may be suited to decreased expenditure on research and development or marketing communications, applying this approach to the whole of the organisation creates an increased risk of being outpaced by competitors in key areas of technology, human resources or marketing.

Finally, the greatest risk posed by the cost leadership strategy is that it is not a universally useful solution, even if potential outcomes of larger market share and higher per-unit margins are universally appealing to managers, shareholders and boards of directors. Cost leadership should not be regarded as an automatic means to improved profit, and should be costed and considered with the same care that would be used for a strategy such as market development or product differentiation.

Porter revisited: assumptions of the cost leadership approach

Porter's value addition strategies are dependent on a series of assumptions regarding market conditions, organisational status, and the interaction of the cost leadership

approach with the rest of the organisation's goals, objectives and strategies. For the most part, these core assumptions are outlined in the definition of cost leadership as being the process of maintaining a relative cost advantage through having a lower total economic cost than the average cost of the competitors in the market (Whitwell, Lukas & Doyle 2003). The assumptions inherent in this definition are that:

- *there are competitors to the organisation*. This underpins the core definition of cost leadership as being relative to market competitors (Whitwell, Lukas & Doyle 2003). This assumption also indicates that the cost leadership strategy can be used in parallel with market development and market penetration.
- *the organisation is competing in a market*. That is, the organisation has products currently available in a market (market penetration) or will use the cost leadership as a method to enter a new market (market development).
- *the organisation has a production process*, which has been refined or improved to deliver the basis for the economic cost competitive advantage. Whilst simplistic, this assumption underpins the need for value chains, and identifies the cost leadership approach as an inappropriate strategy for use with really new products (Chapter 2).

In addition to the assumptions raised by the definition of cost leadership, there are three further areas to consider regarding the application of the strategy. These are that:

- *the investments required to gain the cost benefit will be offset by the profit margin or market share gained*. This is the assumption that underpins the fundamental purpose of the strategy. Organisations need to calculate the total financial cost of per-unit cost reduction in terms of capital, human resources, time, research and development as well as the per-unit costs associated with the creation and delivery of the product.
- *cost reductions can occur without reducing value or utility provided to the customer*. This is the assumption the cost reducing changes will not have a negative impact on the value offering to the customer.
- *cost leadership is one part of a broader marketing strategy*. This is the assumption that the organisation will not be competing solely on reducing internal costs.

Doyle (2002) viewed cost leadership and product differentiation as equally valuable parts of the competitive advantage process. This occurs where an organisation offers something of unique value to the market, at a high price, whilst producing the value offering for the lowest possible cost.

Core principles of cost leadership

Cost leadership is based around the fundamental drive to produce the maximum per-unit value for the minimum possible per-unit cost. In order to adopt the strategy, three areas need to be examined. These are:

- relative cost advantage
- operating costs
- reduced-cost production tactics.

Relative cost advantage

Relative cost advantage is defined by Whitwell, Lukas and Doyle (2003) as being where the organisation has a lower total economic cost than the average total economic costs of its competitors. Total economic cost is defined as the sum of the operating costs plus a charge for capital investment. Capital charges are included in the relative costs advantage to ensure that the organisation does not over capitalise the production process, and effectively create a loss on the production process by having the expenditure on capital absorb any margins gained from the reduced production costs.

In addition, defining relative cost advantage against the market average rather than an absolute of 'lowest cost' allows the organisation a degree of freedom in pursuing this strategy. For example, the organisation can target key competitors, and aim for a relative cost advantage against them, rather than the absolute lowest costs in the market or industry.

Operating costs

Relative cost advantage is also underpinned by control over the operating costs of the organisation. As defined previously, marketing is an organisational function, in which a series of costs are associated with the following areas:

- *value delivery*—the costs incurred in the processes of creating, communicating and delivering value to customers
- *customer servicing*—the cost of managing the customer relationship
- *operations*—the cost of maintaining the organisation as a functional entity that can benefit from the marketing process.

These three broad areas represent the costs associated with the functional elements of the marketing process, rather than the specific business-level cost drivers which are examined as part of the value chain, and the stakeholder contexts below. Cost drivers are the key elements that generate the cost of an activity. Whilst all costs in the organisation are inherently interconnected, as demonstrated in the balanced scorecard and the internal analysis processes (Chapter 4), they can be viewed from a range of different perspectives. In this case, operating costs are examined in terms of how these costs arise in the performance of the marketing function. On the other hand, cost drivers represent broader factors that influence organisational costs, and are not clustered by their role in the marketing process.

Value delivery costs

The value delivery costs are any costs incurred in the process of creating, communicating and delivering value to customers. This usually takes the form of the marketing costs associated with:

- *cost of sales*, including logistics, distribution, and promotions specifically designed to recruit new customers.
- *value creation,* which is the cost of manufacturing the value offering, and includes factors such as the recovery of the investment in research and development.
- *value delivery,* which is the cost associated with the delivery of the value to the customer. Depending on the type of product (e.g. services or goods), it may be either separated from value creation or incorporated as part of the value creation costs.
- *promotion and marketing communications costs*, which are those costs incurred in association with general promotional activity, image enhancement campaigns or other brand enhancement activities.

Value delivery costs are of particular importance in developing a cost leadership strategy and focus predominantly on variable costs (Chapter 5), which can be influenced through factors such as:

- *volume*, where the organisation gains a cost advantage through the economies of scale that occur within the production process. Volume-based cost advantage is particularly relevant when pursuing a market penetration strategy, where the organisation increases the volume of sales to its current markets.
- *the learning effect*, which is related in part to volume, and represents the cost savings that arise from the organisation gaining skill and experience at producing the value offering. For example, this may involve internal innovation where the employees create a more effective or efficient process of creating the product. In the services sector, it can arise from the enhanced skills of the employee gained through experience in the delivery of the service.
- *scope effect*, where cost savings arise through the use of product line extensions that draw from shared organisational resources. For example, colour variations on a basic product will allow for economy of scale to be developed for the internal components of the product, which will be produced at a greater volume than the individual colour cases. The multiple product options can then be presented to the market in the single marketing communications strategy, which shares the costs between the product lines whilst meeting a broader set of customer needs. Overall, by sharing internal components or communications strategies, the total cost can be reduced whilst increasing the range of alternative value offerings to the customer. Scope effect arises from, and is conducive to, market development and product development strategies.

Customer servicing costs

Costs of this type are incurred in the management of the customer relationship, and incorporate the element of marketing expenses that are associated with the development and maintenance of relationships such as loyalty schemes. These are the costs mentioned in the definition of customer lifetime value (Chapter 1). In addition these costs have also been

raised as part of the core customer outcomes measures (Chapter 4) and the lifetime value models proposed by Berger and Nasr (1998).

Cost leadership in marketing relationship costs can be achieved through the scope effect. Scope effects are present where a sales force has a larger range of products to sell to existing markets or customers (Best 2005). As these costs are related to servicing existing customers, cost reduction strategies in customer servicing will impact more heavily on market penetration and product development strategies, which are both based on an assumption that the organisation has already achieved a degree of success in a specific existing market.

Operations costs

The final category of costs considered in marketing performance is the ongoing costs associated with the organisation that is creating, communicating and delivering the value for benefit. These are the broad range of costs that the organisation incurs in the process of its daily operation, such as salaries and capital expenditure. Frequently, these costs are outside of the control of the marketer, and as such, need to be factored into the base cost of the product to ensure sufficient sales revenue to cover the ongoing costs of the organisation.

Reduced cost production tactics for value delivery

There are two areas where marketing strategy can influence the cost component of the product. First, it can manage the relationship costs to maximise the lifetime value of the customer through a combination of cost-management, market penetration, and careful prioritisation of the customers selected for loyalty schemes. These issues have been examined in relationship marketing (Chapter 1), core customer outcomes in internal analysis (Chapter 4), customer analysis in the external analysis process (Chapter 5) and the value of the customer for market penetration (Chapter 7).

Second, there is a range of methods to use in the creation and delivery of the value offering that can influence the cost. These are:

- no-frills approach
- product design issues
- internal efficiencies.

No-frills approach

The no-frills approach to cost leadership is based on offering the most basic product in the market, and relying on it meeting the core needs of the customer at a lower price than that of the competitors (Proctor 2000). No-frills strategies are best suited to product development strategies where the organisation can enter a new product into the market with the reduced feature set. In this approach, competitors with larger or more costly features are committed to continue providing these components to their existing customers. Similarly, plain 'no-frills' products can be used as product line extensions under different brands, or as a specific niche approach to target a segment with a price sensitivity or desire for feature-poor products. The fundamental risk of the no-frills strategy is that it greatly reduces the options for market differentiation and thus can be easily copied by competitors.

Product design

The second aspect of cost reduction in value delivery is inherent in the design and components of the product (Proctor 2000). Product design for cost leadership makes use of the product development process to deliver an equal value offering to the customer at a reduced cost to the organisation. This can be done using several alternative methods including:

- *downsizing the product*, where the value offering is producing smaller units for sale at increased prices. For example, 1.25 litre soft drinks will often sell for less than 600ml drinks. However, because the downsized product is valued in key consumption situations (e.g. drink with lunch or 24-hour availability via a vending machine), a price premium can be charged for the product. Careful control of the distribution and margin costs can increase the profit of the downsized product. In this soft drink case, the consumer will pay twice as much for half of the volume, giving rise to an opportunity for a considerable profit margin.
- *product extensions that provide a reduced feature set*. This is a parallel strategy to the no-frills method; the organisation offers a series of product line extensions that range from those with a low number of features to highly complex alternatives. Where each feature set can be built on the previous component, this creates economies of scale, learning effects and scope effects to reduce costs, whilst complementing a market penetration or market development strategy. For example, Microsoft sells a range of alternative options for the Microsoft Office suite, which reduce the number of component parts (e.g. not offering Microsoft Access for home user packages). As Microsoft has already sunk the cost into the development of the core component parts (Excel, Word, Access, Outlook, PowerPoint), repackaging reduced feature set alternatives provides product line extensions at a reduced total cost.
- *low-cost core components and high-cost augmentation* is where the no-frills strategy is used to manufacture the lowest-cost base unit, and the organisation offers a range of augmentations that can increase the flexibility of the value offering whilst increasing the price. For example, mobile phone packages offer the same basic 'low cost' options of being able to make phone calls and receive messages. These can be supplemented with additional high-cost, high-value augmentation services such as customised ring tones and answering services. This is also the domain of the high-value, low-cost warranty services such as repair guarantees.

As with any part of the marketing strategy process, these mechanisms for cost reduction are interconnected and interdependent on the rest of the organisation's objectives and goals. For example, as illustrated in Chapter 6 (Table 6.3), the effectiveness of a cost leadership strategy is dependent on the financial objectives, internal business objectives and operational objectives of the organisation. At the same time, if the organisation has elected to take a high quality, high price position in a market, it also has to invest in high quality products which may preclude it from using methods such as the no-frills approach.

Internal efficiencies

The third area of the value delivery process is based on the internal efficiencies of the organisation, and these are examined in depth as part of core competencies (Chapter 4), Porter's Value Chain (Chapter 4), market penetration (Chapter 7) and the cost drivers outlined below. Internal efficiencies also draw on the interaction between the stakeholders in the organisation's production context, for example, the dynamics between the organisation and the supply chain where just-in-time manufacturing is used to reduce costs by reducing warehousing and stockpiling. Similarly, where the organisation attempts to lower costs through reducing the size of the workforce, this will be influenced by the union and employee stakeholders.

Managing the cost leadership process

Managing the cost leadership process requires the organisation to set its strategies and objectives around the core principles of efficient value creation, communication and delivery, and the minimisation of extraneous costs. This does not automatically assume that every aspect of the production of the value offering must be done cheaply. Instead, it is an organisational commitment to strategies and tactics that can produce the desired value offering for the target market for the lowest total financial input whilst still delivering value to the customer and benefit to the organisation and its stakeholders. This encompasses three areas:

- *examining cost drivers within the stakeholder context*, where the organisation looks at the areas of common expenditure and determines what factors can be adjusted to create a relative cost advantage for the value offering, and how these interact with the organisation's stakeholders.
- *value chain and cost leadership*, which is the interaction between the primary and secondary value chains and their influence on the total economic cost of the product.
- *cost leadership, value chains and the stakeholder context*, which is the interplay between the drive for relative cost advantage, the role of the organisation's stakeholders, and the dynamics of Porter's Value Chain.

Cost drivers by stakeholder context

As marketing is based on the operation of the organisation for benefit, and the benefit of the stakeholders, cost leadership strategies need to be assessed against the impact they have on the benefit received by stakeholders. More specifically, an analysis of the cost drivers of the organisation, that is, those elements of the operation that create the individual component costs that lead to the total economic cost, should be examined in terms of their interaction with the stakeholders. The four stakeholder contexts raised in Chapter 3 are repeated briefly here. These are:

- *consumption*; the actual purchase and use of the product by the consumers
- *production*, which includes everyone involved in the process, from sourcing the component parts for making the product through to actually creating the value offer or providing the distribution networks

- *environment*, which includes the social norms, acceptable standards and broader community (such as competitors in the marketplace, social pressure groups and the media)
- *regulation and control*, which covers self-regulation and the role of governments in setting legal parameters for the marketplace.

In summary, 16 different cost drivers were identified. These have been grouped together by the stakeholder context in which they arise, or on which they have the greatest impact, to demonstrate how altering the cost drivers will impact on the organisation and its stakeholders.

Consumption context cost drivers

The consumption context presents two areas of cost for the organisation. First, there is the cost of acquiring the sale from a new or existing customer, incorporating the promotion and marketing communications aspects of the value delivery cost. Second, it covers customer service costs including those associated with relationship marketing programs and any difference in the profit margin due to reduced prices paid by 'loyal' customers versus the higher price of the less loyal customer. Both of these aspects have already been discussed.

Environment context cost drivers

The second stakeholder context involves the cost drivers that are external to the firm, and are the result of the conditions existing in the industry or the physical environment. This includes:

- *timing to the market*, which relates to the organisation's position as a market leader (Chapters 2, 6 and 9) or market follower (Chapter 9). This cost factor is also determined by the presence or absence of competitors, another factor outside of the control of the organisation. In terms of cost, being first to market can reduce the costs required to build the organisation's brand, and longer market experience will give rise to cost reductions based on the learning effect mentioned previously. However, second movers and late-to-market organisations can also gain cost advantages from the experiences of the suppliers in developing components for the first mover. Similarly, late-to-market entrants do not have to spend marketing communications efforts on explaining the nature and purpose of the product, and can concentrate on positioning their product against the existing value offering and market demand.
- *location of retailer, manufacturer and distributor*, which are the costs and cost benefits based on the physical location of the organisation in regards to the supply, distribution and retail channels. This ranges from the benefits of the position of the organisation's retail outlets, through to the costs associated with any rent premiums paid for prime real estate space. Cost drivers from this aspect also interact with the supplier and distributor costs of the production context.
- *marketing costs*, which incorporate aspects of the consumption costs, but specifically refer to the costs required to equal or better the marketing communications of the organisation's competitors.

Production context cost drivers

The production context is the broadest category of stakeholders, and consequently, the broadest collection of cost drivers. Effectively, this covers the entire cost incurred within the organisation's efforts to create, communicate and deliver value to the consumers. It also integrates most closely with Porter's value chain concept, which is explored in more depth later in the chapter. The core cost drivers of the product context are:

- *capacity utilisation*, which is the cost benefit that comes from the optimum use of the organisation's capital equipment or service provision capacity. Factors that influence the capacity utilisation include cyclical demand (peak hour commuter demand for transport) and season fluctuations (e.g. peak demand for resorts in summer). Increased use of the organisation's capacity through growth strategies, use innovations or demand management can also reduce the per-unit cost of the charge for capital, which is incorporated into the calculation of relative cost advantage (Whitwell, Lukas & Doyle 2003).
- *distribution channels*, which involves the costs associated with the delivery of the value offering to the customer, and includes the interaction between the organisation and the distributor stakeholders. Distribution can also be influenced by the environment context costs depending on the costs associated with servicing the location of the target market. For example, regional areas have high distribution costs due to their distance from the main production facilities. Altering the environment cost by placing a product facility into a regional area will also alter the distribution costs.
- *economies of scale*, which have been mentioned previously, and which arise where discounting can be achieved through the volume of products being produced. However, economies of scale are only financially beneficial for cost-reduction where they are also tied to the market demand for the product. For example, where market demand is only 300 units, ordering 1000 units to achieve an economy of scale will result in the cost of 700 wasted units.
- *experience and innovation in the production process*, which can be used to lower the cost of production, and which partially contributes to the costs associated with new-to-the-organisation product development. This aspect ties into the management and employee stakeholder context where the organisation needs to retain skilled and experienced workers in order to effectively make use of production process innovation. Cost reductions through experience have been mentioned previously as part of the learning effect and internal efficiencies.
- *horizontal and vertical integration*, which is where the organisation attempts to reduce costs by acquiring the supply chain and/or the distribution channels to incorporate the entire process into a single organisation. Similarly, this can also represent the desire by the organisation to outsource supply, core component manufacturing or product distribution as a means to reduce costs. This ties into

the supplier and distributor stakeholders, although it can also impact on the employee and union stakeholders where the firm looks to outsource these functions.

- *interrelationships between production processes*, which is where shared production processes reduce costs by achieving economies of scale on raw materials and components or through increasing capacity utilisation.
- *labour costs*, which is the financial cost of employees, managers and any staff involved directly in the primary value creation. Whilst reducing labour costs tends to result in improved conditions for shareholders, cost cutting that causes the loss of skilled staff will reduce the organisation's overall savings by decreasing the cost reductions to be gained from the learning effect. Labour costs are most closely aligned to the union, management and employee stakeholders, although cost reductions in this area can positively influence shareholder value by the organisation being rewarded in the stock market for 'trimming the fat' and apparently becoming more efficient.
- *linkages between costs and savings*, which is where expenditure on one aspect of the system produces greater savings later in the process. For example, spending above industry average costs on staff to acquire the highest skilled employees can contribute to savings from increased product quality and performance, and can generate improved customer satisfaction. Similarly, reducing costs by purchasing cheaper raw materials that lead to greater wastage due to spoilage or product failure can prove to be a false economy. In this manner, cost leadership is a holistic 'whole of system' approach to reducing cost, rather than just focusing on each part of the value chain as an isolated component.
- *policy choices*, which represent the decisions by the stakeholders, boards of directors and managers as to which method of cost reduction will be pursued. This factor covers the costs that arise from the interaction of the current strategy with the whole of the firm's objectives and goals. For example, if the firm is focusing on a cost leadership strategy by reducing investment in research and development, this policy choice will impact on the ability of the firm to produce lower-cost products through utilising changes in production technology or developing new methods of delivering the core value to the consumer.
- *raw materials*, which relates to the costs that arise from the component parts of the organisation's value offering. This interacts with other factors such as the quality of the end product, power of suppliers and the volume of materials being purchased, which is in turn influenced by the number of products that use the same component.
- *reduction of overheads*, which is the cost of the second tier of the value chain, and relates to any and all internal costs that are associated with the operation of the firm. This was covered previously in the chapter as the operating costs.

Cost drivers within the production context are frequently interdependent, and changes to one aspect of the production system can have repercussions for cost drivers in other areas of the firm. For example, reducing costs through economies of scale will impact on the level

of raw materials required, the distribution costs of shipping the increased production volume, the utilisation of the organisation's production capacity, and the possible need to increase the workforce to reach the required production level. Where possible, the foreseeable impact on all of these factors has to be costed to determine if targeting one cost driver (e.g. economy of scale) will result in a relative cost advantage or will increase overall costs due to follow-on costs (e.g. capital investment or high materials costs).

Regulation and control context cost drivers

Institutional factors such as the costs imposed by government, regulation, taxes or restrictions are the final influences on cost leadership strategy. For example, a government mandated curfew can limit the operation of an airport, and decrease the opportunity to utilise the full capacity of the infrastructure. Similarly, mandatory safety requirements or environmental policies may increase the cost of the production process. Alternatively, government policy may decrease organisational costs through the provision of subsidies, tax relief, or having the government bear part or all of the cost of key infrastructure such as port facilities or rail lines.

Value chain and cost leadership

Porter's Generic Strategies of cost leadership and differentiation (Chapter 11) are interconnected with Porter's value chain concept. In review, the value chain is a conceptual model of the organisation as a holistic entity where each value adding component activity is linked to the final value offering by the firm. All activity in the organisation can then be seen as contributing aggregate value to the consumer and contributing to the aggregate cost incurred by the firm. As outlined previously in Chapter 4, the model splits the activities of the organisation into primary value creation and the secondary components (Viljoen & Dann 2003; Hooley, Saunders & Piercy 2004, Porter 1985). The primary value creation chain consists of the following elements:

- *inbound logistics*, which is the process of managing the input flow of resources into the company.
- *operations*, which is the process of turning the input into saleable value offerings for the customer.
- *outbound logistics*, which represents the assembly, processing, storing and shipping of the product to the consumer or the distribution channels.
- *sales*, which represents the communication of the value offering to the customer, and the value exchange process.
- *service*, which is the after-sales augmentation of the physical product's value offering or the delivery of the service product's value.

The secondary value creation chain represents the supporting elements of the organisation and involves the areas of:

- *procurement*—the process of acquiring the resources needed for each of the value-adding components of the value chain

- *technology development*—the process of ensuring that the technology used by the value-addition processes has the best fit with the organisation
- *human resources*—the capacity of the organisation to ensure the right sets of people, skills, abilities and motivation are available to the organisation as employees, contractors or other participants in the production process
- *systems*—the efficient and effective operation of the organisation through the management and control of organisational processes, systems and procedures
- *marketing*—the organisation's coordinated efforts to define 'value' in terms of how the customer perceives it, and creating a value offering that meets the customer's needs and wants.

However, Porter's model does not incorporate all of the cost drivers that influence the organisation's total economic cost. There are three additional cost drivers external to the organisation, and therefore outside of the value chain. These are:

- timing to the market
- location of retailer, manufacturer and distributor
- institutional costs/government costs and subsidies.

Table 10.1 outlines the interconnection between the elements of cost drivers and the value chain.

Table 10.1 provides a summary of the areas of interaction and interconnection between the value chain and possible areas that can be used for cost leadership. This also allows for the re-use of knowledge and insight gained in the internal analysis (Chapter 4) where the value chain was initially assessed. Further, this process can be used to examine if the areas covered by the cost drivers can be manipulated to improve the organisation's overall performance in the value chain, both for cost leadership and for product differentiation (Chapter 11).

Leadership value chains and the stakeholder context

In addition to the connection between Porter's value chain and the cost drivers, there is also an interaction between the four areas of stakeholders, Porter's value chain and the respective cost drivers. As marketing fundamentally requires organisational and stakeholder benefit, the pursuit of this outcome can be enhanced through the application of the value chain analysis (Chapter 4), and the exploration of changes that could be made to the organisation's cost drivers. Similarly, attempts to alter the cost structure of the organisation as part of the cost leadership marketing strategy should also be examined to determine if it will adversely impact a key stakeholder group. Table 10.2 outlines the summary interaction and interconnection of the cost drivers, stakeholders and the value chain.

Overall, the purpose of examining these interactions and interconnectivity is to demonstrate that marketing strategy needs to be a holistic approach to the organisation and its stakeholders. Cost leadership may have initial appeal for the balanced scorecard's financial objectives (Kaplan & Norton 1996) but after examining the impact of the

TABLE 10.1 **Cost drivers and Porter's value chain**

Element	Primary value chain	Secondary value chain
Cost of acquiring the sale from a new or existing customer	Sales Service	Marketing
Cost of servicing the existing customer	Service	Marketing
Marketing costs	–	Marketing
Capacity utilisation	Operations	Procurement Technology development Systems
Distribution channels	Outbound logistics	–
Economies of scale	Operations	Technology development Systems
Experience and innovation in the production process	Operations	Technology development Human resources Systems
Horizontal and vertical integration	Inbound logistics Outbound logistics	Procurement
Interrelationships between production processes	–	Systems
Labour costs	Operations	Human resources
Linkages between costs and savings	–	Procurement Technology development Systems
Policy choices	–	Procurement Technology development Human resources Systems
Raw materials	Inbound logistics	Procurement
Reduction of overheads	–	Procurement Technology development Human resources Systems Marketing

TABLE 10.2 Interconnection of cost drivers, stakeholders and the value chain

Cost driver	Context	Stakeholder	Primary value chain	Secondary value chain
Cost of acquiring the sale from a new or existing customer	Consumption	Customers	Sales Service	Marketing
Cost of servicing the existing customer	Consumption	Customers	Service	Marketing
Timing to the market	Environment	Competitors	–	Marketing
Location of retailer, manufacturer and distributor	Environment and production	Local community Society Social pressure Groups	Operations	Procurement Technology development Systems
Marketing costs	Environment	Competitors	Outbound logistics	–
Capacity utilisation	Production	Employees	Operations	Technology development Systems
Distribution channels	Production	Distributors	Operations	Technology development Human resources Systems
Economies of scale	Production	Employees Suppliers	Inbound logistics Outbound logistics	Procurement
Experience and innovation in the production process	Production	Managers Employees	–	Systems
Horizontal and vertical integration	Production	Suppliers Distributors	Operations	Human resources

Interrelationships between production processes	Production	Employees Managers	–	Procurement Technology development Systems
Labour costs	Production	Union Employees Management	–	Procurement Technology development Human resources Systems
Linkages between costs and savings	Production	Managers Creditors and financiers Suppliers	Inbound logistics	Procurement
Policy choices	Production	Shareholders Managers Board of Directors	–	Procurement Technology development Human resources Systems Marketing
Raw materials	Production	Suppliers		
Reduction of overheads	Production	Employees Managers Suppliers		
Institutional costs/ government costs and subsidies	Regulation and control	Government		

strategy on the stakeholders and the value chain, it may not prove to be the optimum method for the organisation to pursue. Without investigating the interactions and interconnectivity, the inherent appeal of increased margins or market share through decreased costs may override the standard level of caution required before implementing any marketing strategy.

Conclusion

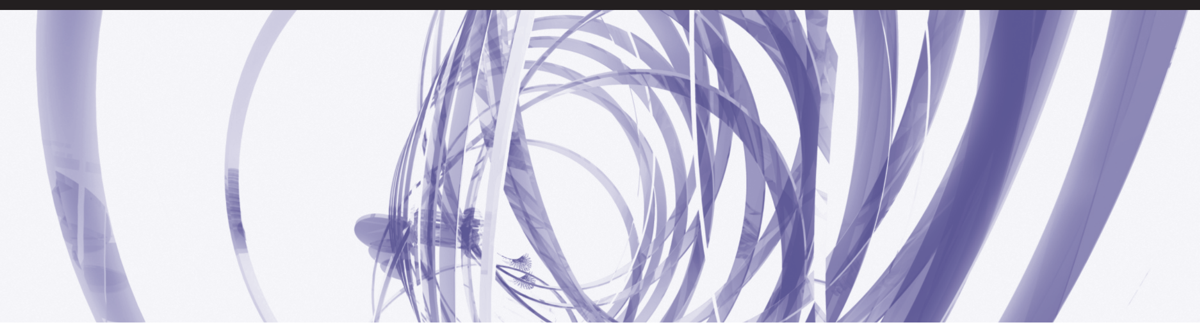
Cost leadership is one of the key generic strategies used to underpin sustainable competitive advantage, however its application is often misunderstood. Cost leadership does not necessarily result in price leadership. Cost leadership can be pursued independently of the external positioning of the product and the organisation in the market. High perceived quality products, sold by companies of high reputation and commanding relatively high prices in the market may, from a production perspective, be cost leaders. There is no obligation on the part of the organisation to translate cost leadership into low prices although this is always an option.

As part of the holistic strategy of the firm, cost leadership operates in parallel with strategic growth strategies (such as market penetration) by providing a buffer to absorb increased costs associated with growth or product development by providing an internal source of investment funds to cross-subsidise new products from the profits of existing high-margin products.

Despite its intuitive appeal, cost leadership, like any strategic option, is not always the optimum strategy to pursue. Organisations that do choose to pursue cost leadership need to consider the decision in the light of the full range of internal and external pressures from stakeholders as well as the organisation's capacity to benefit from components of the strategy (such as economies of scale and sharing of production facilities across product lines). There can only be one cost leader in any given market segment. While organisations can and should pursue strategies which minimise waste and inefficiencies, thereby improving the cost base, the overall generic strategy they pursue will often take another form.

Value addition and strategic competitive advantage 2—Product differentiation

CHAPTER 11



Introduction

Product differentiation strategy is based on presenting to the target market a unique value offer that provides the organisation with a relative competitive advantage for serving the needs of the customer. As a business strategy, it has to meet the organisation's needs of profitability and sustainability. As a method of satisfying customer needs, it has to provide a product that differs from the competition on some salient point and that point has to be something the consumer desires. The overall aim of product differentiation strategy is to develop a product focused on relative competitive advantage. To do this, the differentiated features of the product must provide the target market with a value that is relevant and meaningful, and do this in a manner that gives benefit to both the organisation (differentiation advantage) and the customer (unique value). This chapter overviews the concept of value as perceived by the customer, and the role of the differentiation strategy in creating a competitive advantage for delivering greater value to the customer for the benefit of the organisation and its stakeholders.

Establishing differentiation

There is a core set of specific outcomes required from an organisation attempting to use a product differentiation strategy (Hooley, Saunders & Piercy 2004; Proctor 2000). Value offerings under consideration as part of a product differentiation strategy must include the following features:

- *the differentiation must be perceived to be valuable by the customer*, which places the dominant emphasis of the strategy on the role of consumer behaviour, market research and understanding the needs of the market.
- *the point of differentiation must create value for the customer*, which reinforces the need for the product differentiation to be seen to be valuable, and to actually deliver utility to the consumer.
- *the differentiation needs to be unique*, which makes the difference between the organisation's product and competitor value offerings meaningful to the consumer.
- *the differentiation must be difficult to copy*, which ensures that the point of difference remains a point of difference, and is not quickly matched by competitors.
- *the differentiated product or message must be aimed at a tightly defined market*, which is related to the need for the customer to perceive and receive value from the point of differentiation.
- *differentiation strategies have to be linked to the customer*, which means the changes to the product must be to meet the needs and the demands of the market. Adding features without assessing the value of these features for the customer is not a differentiation strategy.

Tactical value of product differentiation

The primary tactical value of product differentiation is that it presents a reason for the consumer to purchase the organisation's product (Hooley, Saunders & Piercy 2004). Differentiation places the emphasis on the utility and value the consumer receives from the organisation's value offering ahead of factors such as price. Well-executed differentiation strategies can increase price tolerance by emphasising the benefits of the value offering.

Differentiation also aims to be industry-wide or market-wide and is based on factors such as branding, quality or innovation. This distinguishes it from niche strategies, which are focused on delivering a value offering to a narrowly defined single market segment (Chapter 12).

Ultimately, the purpose of product differentiation is to demonstrate to the consumer that the organisation's value offering has a relative competitive advantage over the products offered by its competitors because they offer the client greater utility.

Risks of product differentiation

As with the cost leadership strategy, there are risks inherent in the application of product differentiation. The key risk is the organisation's self-perception of the value offering as

being unique, or of inherent value to the consumer. Whitwell, Lukas and Doyle (2003) noted that companies that have failed product differentiation strategies frequently overstated their product's uniqueness compared to the present market offerings. Even if a product has additional features that make it 'unique', it is the *perception* of the relative value and differentiation of the total product offering on which consumers base their acceptance or rejection of the strategy. Hooley, Saunders and Piercy (2004) outlined a series of generic risks associated with the product differentiation. These are:

- *competitive advantages are not static or permanent*, that is, the factors that made the product unique initially quickly become expected components of the value offering from the organisation. Similarly, differentiation based on the features of the product may be imitated by competitors, whilst differentiation based on social factors such as prestige or image are subject to shifts in fashion and taste.
- *differentiation can be imitated*. Although differentiation aims to produce a unique product offering, given enough time, money and desire this offering can be replicated by competitors.
- *differentiation can have high levels of cost*. The initial investment in the development of the competitive edge for the product often requires an unbalanced future-focused portfolio (Chapter 4). Heavy investment in product design, market research and the development of the value offering may also preclude the use of a cost leadership strategy in parallel with product differentiation. Further, the costs inherent in creating product differentiation may outweigh the projected revenue from the revised product.
- *differentiation often depends on new technology*, which either can be purchased from external suppliers, or needs to be developed inside the organisation. Technology developments often overtake an organisation, and the 'cutting edge' feature that was the selling point of the differentiation strategy may be made redundant by shifts in the technology.

Product differentiation also carries the inherent risk of altering the perceived value offering to the market by emphasising a specific element of the product which, whilst designed to increase market share, may conflict with a market penetration or relationship marketing strategy. For example, a prestige product which is positioned on a distribution differentiation strategy would damage the brand by making it more accessible to the wider market. Similarly, technology-driven products which derive their differentiation from the complexity of their feature set (e.g. high-end mobile phones and personal digital assistants) would lose their core market if the differentiation strategy were altered to emphasise simplicity.

Assumptions of the product differentiation approach

As with all forms of strategy, product differentiation is underpinned by a range of assumptions regarding the market, the organisation and the consumer. In product differentiation,

the customer receives a product that provides a unique series of benefits, whilst the organisation meets its goals of offering a product for its benefit, and the benefit of its stakeholders.

The key assumptions underpinning this process are:

- *the assumption of utility*, in which the organisation assumes that the differentiation will provide value to the customer.
- *the assumption of advantage*, where the organisation has the belief that its value offering has a relative advantage over the competitor's offerings.
- *the assumed existence of competitors and markets*, which underpins the 'relative' aspect (the competitive advantage being assessed against other alternatives inside a market).
- *the assumption of a current product or the development of a new product for an existing market*, which is related to the previous assumed existence of competitors and markets. Varying levels of differentiation can be used within market development and market penetration strategies, however differentiation is precluded from diversification strategies that create new products for new markets (Doyle 2002).

The exclusion of the diversification strategy and the new-to-the-world style products from the product differentiation strategy is based on the fundamental need of the differentiation strategy to provide a relative competitive advantage to that of the organisation's competitor products (Cohen 2001).

Customer utility: providing value to the customer

Product differentiation is heavily grounded in two areas of interaction with the consumer. First, the differentiating feature must be based on the needs of the consumer, and second, it has to be provided within a cost or price framework that is acceptable to the consumer. Consequently, product differentiation strategies have to be designed around increasing the utility of the product for the consumer. Before determining what utility a product will offer the market, it is first necessary to ascertain what constitutes utility and value from the consumers' perspective. There are two key theoretical models which examine consumer value:

- *Kaplan and Norton's (1996) value proposition analysis*, which examines the value the consumer is currently experiencing from the organisation's products and services
- *Doyle's (2002) utility equation*, which examines the consumer's perception of the value that they could experience from the differentiated product.

Kaplan and Norton's value proposition

In Chapter 4, Kaplan and Norton's (1996) value proposition was used as part of the analysis of the organisation's relationship with the customer. The information gathered as part of the internal analysis of current customers can be used in the development of a product differentiation strategy. Value is defined by the value proposition equation:

Value = Actual product or service attributes + Perceived image + Relationship with the organisation

Product/service attributes are the current capacity of the organisation's product or service to meet a customer's need or want, and consist of four subcomponents:

- *functionality*—the extent to which the product actually performs the task required to meet the needs
- *quality*—the subjective level of satisfaction with the intangible elements of the performance, and the worth or value level of the component elements of the product
- *time*—incorporating the amount of effort, energy and forgone opportunities required to have the need satisfied by the organisation's product
- *price*—representing the financial cost of the product to the consumer, plus the non-financial costs of social influence or pride.

The second part of the value proposition, perceived image, refers to intangible factors including:

- *perceived quality*—the subjective opinion of the consumer regarding the quality of the product
- *organisational reputation*—based on the total of the organisation's behaviour including any negative publicity or corporate scandals
- *branding strategies*—how the specific product is sold to the market, which include:
  - *marketing communications*, which are the marketing messages that have communicated the details of the value offering to the consumer
  - *positioning strategies*, which located the product in the marketplace and in the mind of the consumer.

The third and final component of the value proposition equation is the relationship the customer has with the organisation. This includes factors such as:

- *satisfaction*—the consumer's experience of the delivery of the value offering and whether it met, failed or exceeded the consumer's needs
- *interaction with the organisation*—the consumer's experience of dealing with the organisation during the sales process, and any after-sales service interactions
- *intention to continue the ongoing relationship*—how the customer feels about buying from the organisation in the future.

The Kaplan and Norton (1996) model provides the starting point for the differentiation analysis. It provides a benchmark of the organisation's current value offering to the market, and how it is perceived by the consumer. The next step for the organisation is to review the value offering sought by the market through the use of the Doyle (2002) utility equation.

Doyle's utility equation

In contrast to Kaplan and Norton's (1996) approach, which benchmarks the current product experience, Doyle's (2002) approach examines the consumer's perception of the potential

value they could receive from the product. Value was defined by Doyle as being the difference between the utility the consumer perceives they will gain from the product and the costs they believe will be associated with its use. For differentiated products, the utility question is further complicated by the consumer needing to perceive increased utility from the differentiated product ahead of the utility of the competitor's offerings. The components of utility are illustrated in Doyle's utility equation:

Differentiated product value = Perceived increased utility – Perceived cost

Perceived increased utility in Doyle's equation consists of the consumer belief of the product or service's improved effectiveness according to the following criteria:

- *personal benefit*: can the consumer see a direct and personal benefit from using the differentiated product ahead of alternative value offerings?
- *performance*: does the consumer perceive the differentiated product to be offering superior performance in comparison to the product they are currently using?
- *features*: does the differentiated product include new features that are meaningful, useful or valuable in the eyes of the consumer?
- *service*: does the differentiated product include a new service that the consumer sees as useful?
- *quality*: does the differentiation strategy used on the product alter its perceived quality in the opinion of the consumer?
- *availability*: will the differentiation strategy alter consumer access to the product in a useful, valuable or meaningful way?

The key to increased perceived utility is that it has to come from the consumer's perspective, rather than from the organisation. Whilst many parts of this chapter examine product differentiation from the organisation's perspective, the ultimate goal is to demonstrate an increase in one or more of the perceived utility factors used by the consumer. As part of the consumer focus, the organisation also needs to consider the consumer's perceptions of the cost of using the product. Doyle (2002) and Wood (2004) identify five areas of perceived cost:

- *initial purchase price*, which is the monetary cost of the value offering
- *cost of use*, which relates to any ongoing monthly fees, service charges or other costs which are not related to the consumable goods or ancillary product
- *cost of ancillary products*, which include the consumable goods required for the use of the product (e.g. fuel for cars, paper for printers) and any supporting products (software for computers) that enhance the utility of the product
- *maintenance and repair costs*, which is the cost of keeping the product in an adequate working condition (e.g. car servicing)
- *non-financial operating costs*, such as the time required to use the product or service, the difficulty or ease of use, and other social factors such as pride or social reputation.

Perceived cost in this context is what the consumer feels they will have to spend, rather than what the consumer actually will incur in the way of costs. Consequently, the consumer may overestimate costs for products they are unfamiliar with, or ascribe non-existent costs to the value offering. For example, a consumer may not purchase a differentiated all-in-one computer product on the assumption that they will have to pay regular monthly fees to use the software on the PC. Alternatively, they may assume that the added electricity costs of running the differentiated high-end computer would be prohibitive, and decide against the purchase, even though the total electricity consumption would not be noticeably higher. This is where the product development model's concept testing and test marketing aspects (Chapter 9) can be used to assess the consumer's attitudes to the differentiated product.

Core principles of product differentiation

From the organisational perspective, product differentiation is based on finding a method of demonstrating the superiority of the value offering to the consumer. This is examined through four areas:

- differentiation for relative competitive advantage
- types of relative competitive advantage
- four levels of product differentiation
- checklist for differentiation.

Differentiation for relative competitive advantage

The value of product differentiation is that it provides a reason for the consumer to purchase the organisation's offering ahead of competitor products. In Chapter 10, the cost leadership strategy focused on producing a relative cost advantage, defined as being where an organisation has a lower total economic cost than the average of the competitors in the market (Whitwell, Lukas & Doyle 2003). Relative competitive advantage works on a similar principle of being a superior alternative to the average competitor's product in a given market. In this way, the organisation can focus on offering relative advantages across different segments, and against different competitors. Further, relative competitive advantage removes the need for the organisation to attempt to be the market leader in all categories. Instead, it allows for greater focus by being the relatively preferred alternative in a given market segment.

Types of relative competitive advantage

Relative competitive advantage exists on a continuum from the tangible to the conceptual. Tangible advantage incorporates the physical aspects of the product. Tangible advantage is relatively easy to copy and hard to sustain as a point of differentiation. In contrast, conceptual advantage is hard to copy as it represents a person's mental associations with the product. In the middle is the intangible advantage that mixes the physicality of the tangible advantage and the experiential aspect of the conceptual advantage in service delivery and relationship marketing features. Whilst these can be copied, services are

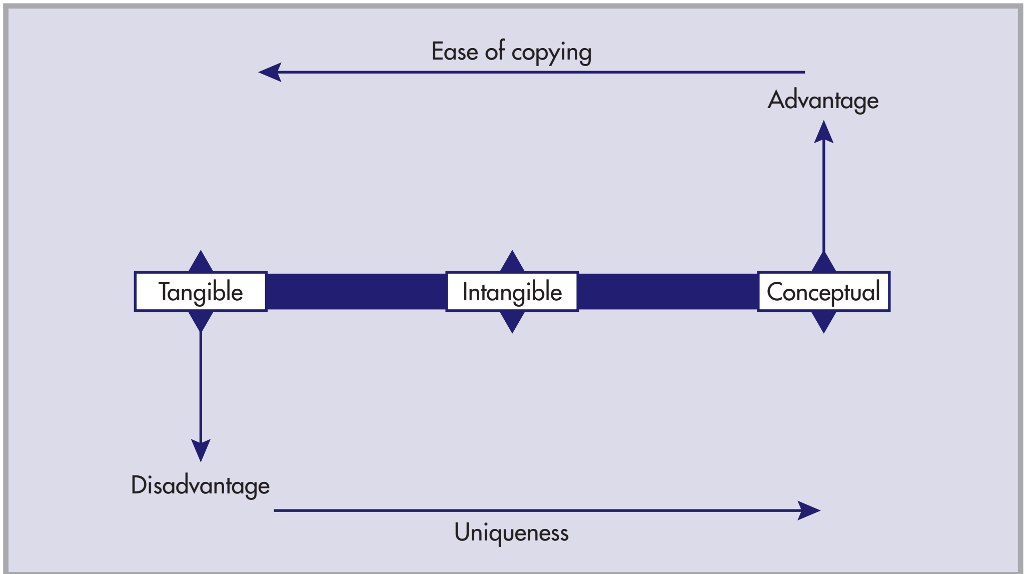


FIGURE 11.1 **Relative competitive advantage continuum**

difficult to replicate, particularly where the service provision is based on the skills or personality of an individual provider. Figure 11.1 demonstrates the continuum of the relative competitive advantage.

As illustrated in the figure, there are three basic forms of relative competitive advantage. These are:

- *relative tangible advantage*, where the organisation's value offering has a physical component that can deliver a superior value offering. This includes aspects from Doyle's (2002) utility equation of features, quality and performance, and also includes Kaplan and Norton's (1996) 'actual product/service attributes'.
- *relative intangible advantage*, where the organisation can offer a set of personally deliverable skills and service performance that are superior to those offered by the competitor. This interacts with Doyle's (2002) utility equation component of service, and Kaplan and Norton's (1996) 'relationship with the organisation'.
- *relative conceptual advantage*, where the organisation's brand, image, reputation, positioning strategy and integrated marketing communications (IMC) create a social message that is attached to the organisation's value offering and that is valued by the consumer. Conceptual advantage is compatible with Kaplan and Norton's 'relationship with the organisation', and with the 'perceived image' aspect of their value proposition equation.

These forms of advantage also interact with Doyle (2002)'s drivers of utility, which are examined in greater detail later in the chapter. Relative competitive advantage does not require the organisation to have an advantage on each of the three axes—it is possible for the organisation to hold a relative conceptual advantage through branding and positioning

for a product that has no physical advantage or service advantage. Similarly, physical advantages can exist independently of brand reputation or advantage.

However, whilst there are three competitive advantage positions, it is also possible for the organisation to hold one or more of the three relative competitive disadvantage positions. These are:

- *relative tangible disadvantage*, which is where the competitor offers a superior range of features, quality or other performance measures.
- *relative intangible disadvantage*, which is where the organisation's service offering or relationship marketing does not equal or better the competition.
- *relative conceptual disadvantage*, which is where the organisation has limited brand awareness, a poor product or organisational reputation, or is perceived to be out-performed by rivals.

Relative competitive disadvantages need to be considered as part of a set of tactical and strategic decisions. Given that the value of product differentiation is solely determined by the perception of the consumer, and the consumer's willingness to purchase the product based on those perceptions, the competitive disadvantage may not always be detrimental to the organisation. For example, if the market segment places a value on the physical features of the product, a conceptual disadvantage can be outweighed by the performance of the product. In reverse, the tangible disadvantage of not being the most technically superior product offering did not stop the mp3 file format from becoming the default standard for digital music. Given the complexity of value offerings as bundles of tangible products, intangible outcomes and conceptual ideas, it is also vital to assess where the differentiation occurs within the different levels of the value offering.

Four levels of value offering differentiation

Value offerings exist at four possible levels from the core value that is provided to the consumer, through to the extended potential or 'what-if' capacity of future products. These four levels (outlined by Hooley, Saunders & Piercy 2004) are:

- *core product*, which is the basic benefit provided to meet the needs of the consumer. Core products are best differentiated through tangible and intangible components, however, where the core value offering is the social message sent by ownership of the product (e.g. fashion), the core product can be a conceptual advantage.
- *expected product*, which is the minimum level of features and benefits that the market expects from a product of this type. The expected product level is akin to anti-differentiation insofar as any product lacking in the expected feature set is likely to have a relative competitive disadvantage.
- *augmented product*, which is the benefit set not usually associated with the product. Augmentation of the product can occur through the three levels, and can be used, for example, to add intangibility to a tangible core product or to provide a

conceptual advantage to the tangible and intangible products. Similarly, tangible products can be used as a physical demonstration of the social message of core conceptual product—for example, wearing a Harley-Davidson-branded watch serves to reinforce the conceptual position of the motorcycle brand, and the social messages associated with a Harley-Davidson owner.

- *potential product*, or the possibilities presented by the product for the future, represents either additional desired features, or a sense of future reward from the value offering. Where potential products are focused on possible future social meaning, they represent the opportunity to develop a conceptual advantage for the brand. For example, fashion-seeking consumers may adopt an unknown brand or designer as an investment in the future social message.

Table 11.1 outlines potential areas of consumer utility and value to be gained from a relative competitive advantage in each of the core, expected and augmented product.

TABLE 11.1 Relative advantage, value offering and consumer utility/benefit

		Relative advantage	
	Tangible	**Intangible**	**Conceptual**
Core product	Personal benefit Utility	Personal benefit Utility	Personal benefit Utility Value
Expected product	Performance Features Availability Actual product features Quality	Performance Service Availability Actual service features	Value Utility Perceived image
Augmented product	Performance Features	Service Relationship with the organisation Quality	Perceived quality Value Utility Perceived image
Potential product	Use innovation	Performance Use innovation	Perceived image

Value offering checklist

The final principle of differentiation is the Hooley, Saunders and Piercy (2004) checklist for the organisation's value offering. This three-item checklist should be used when reviewing the value offering being presented as a product differentiation strategy. The three questions are:

- *What does the customer expect in addition to the core product?* This question allows the organisation to check if any tangible, intangible or conceptual elements of the expected product are missing, or have been mistakenly identified as points of differentiation.
- *What does the customer value in addition to the core product?* This question examines what additional benefits can be added through augmented or future products that would give a competitive advantage to the organisation.
- *How easily can the differentiation be copied?* This is a twofold measure of the uniqueness of the differentiation and the expected lifespan of the advantage before it becomes part of the expected or core product.

Creating differentiation

Having assessed the role, purpose, value and importance of the consumer in product differentiation, it is also important to examine how to implement a differentiation strategy in order to create a relative competitive advantage. Initially, the first step in product differentiation and competitive advantage is to benchmark the current product through the Kaplan and Norton (1996) measures (Chapter 4). Second, the product differentiation process relies on the analysis of the needs of the market, which was part of the external analysis (Chapter 5), the policy matrixes (Chapter 3) and organisational objectives (Chapter 6). Having established the benchmark, market demand and organisational direction, the product differentiation strategy requires:

- *the identification of the appropriate mechanisms for differentiation*, which is where the organisation adjusts aspects of the marketing mix to create and communicate the differentiated offering.
- *the identification of any changes to the value chain required by the previous step*, which involves examining the impact of the proposed differentiation strategy on the internal organisational process.
- *the examination of the consumer's drivers of utility*, which is where the proposed differentiation value offering is examined against the consumer's needs and wants.

Mechanisms for differentiation

As with most aspects of strategy, there is no one 'universal' template for determining the implementation of strategic objectives. To complicate matters for product differentiation, the nature of relative competitive advantage is that the organisation's differentiation strategy is codependent on the actions of its competitors. Similarly, the need to target the consumer directly to provide meaningful utility with the differentiated product means that few, if any, differentiation strategies will be alike. There are two main clusters of product differentiation mechanisms:

- *marketing mix mechanisms*, which are based on presenting differentiation through adjustments to the 4Ps (price, product, place and promotion) of the marketing mix

- *marketing outcomes mechanisms*, in which the differentiation is based on the outcomes of marketing (such as branding, packaging, perceived quality and the sales effort).

Marketing mix mechanism

Although the marketing mix has seen more than its fair share of criticism over time, it still forms a useful framework for assessing potential areas for distinguishing the organisation's value offering from that of its competitors. The four core marketing mix variables are:

- *price*, which is where differential advantage is derived from either being the lowest priced through an aggressive cost leadership strategy (Chapter 10), or through premium price positioning in conjunction with branding (Hooley, Saunders & Piercy 2004; Whitwell, Lukas & Doyle 2003). Price alone is the easiest form of differentiation to copy. However, when psychological pricing is used to reinforce branding, positioning and perceived quality, it becomes an integral, and unique, aspect of the product's relative conceptual advantage.
- *product*, which represents the mechanism for delivering the value offering to the consumer, and consists of the features that the organisation uses to deliver benefit to the consumer. Modifying the physical product is usually core to the differentiation strategy, and should be assessed through the product development process (Chapter 9). For the most part, this chapter has focused on the adjustment of the product design to create a differentiation advantage to communicate to the target market.
- *promotion* or *marketing communications*, which relates to how the organisation communicates the differentiated value offering to the market. It also includes the extent to which marketing communications create social messages regarding the use and value of the product, and to what extent these messages can be beneficial to the consumer's self-image. Hooley, Saunders and Piercy (2004) identified factors such as message style, content and frequency, along with public relations and publicity, as key areas where the organisation could provide differentiation for relative conceptual advantage. This area is also tied to the marketing effort mechanism elements of branding.
- *place or distribution*, which is where the availability of the value offering sets it apart from competitor products. This can be by enhancing the perceived quality of the product through exclusivity and high quality distribution outlets. Alternatively, it can be used to differentiate the product by providing wider availability than competitor alternatives.

Table 11.2 outlines possible areas of interaction between the differentiation mechanism and Doyle's (2002) perceived utility, Kaplan and Norton's (1996) value proposition, the relative competitive advantage and Hooley, Saunders and Piercy's (2004) product level.

Marketing outcome mechanism

Differentiation can also occur as an outcome of the marketing efforts of the organisation, specifically in respect to the marketing communication strategies mentioned previously,

TABLE 11.2 **Marketing mix mechanisms**

Differentiation	Perceived utility	Value proposition	Relative advantage	Product level
Price	Nil	Price Perceived quality Branding strategies	Conceptual	Nil
Product design	Personal benefit Performance Features Service	Functionality	Tangible Intangible Conceptual	Core Expected Augmented
Marketing communications	Personal benefit	Perceived image Organisational reputation Branding strategies	Conceptual	Augmented
Distribution	Availability	Perceived quality Interaction	Tangible Intangible	Core Expected

and other factors such as differentiating the product through packaging. The four areas of primary influence are:

- *branding*, which includes brand leadership and brand awareness, along with the social message conveyed by association with the organisation's brand. Branding acts as a relative intangible and conceptual advantage, with distinct interaction with the consumer's perceptions and the conveyed social message. Differentiation through branding relies on creating a brand that has the following features:
  - *a memorable hold on the market*, making it both readily identifiable and unique
  - *a role as a quality statement*, where the brand conveys the relative quality of the value offering by association
  - *value for money symbol*, indicating that the presence of the brand mark is indicative of prior positive experiences with the utility of the product
  - *acts as a social message shortcut*, which is to say that the entirity of the relative conceptual advantage message can be conveyed in a single logo or brand mark that will be recognised and interpreted by consumers.
- *packaging*, which incorporates the physical medium used for the distribution of the value offering. This includes an advantage that can be derived from differentiating the value offering in terms of:

- — how the product can be stored
- — what level of protection the packaging provides for the value offering
- — what image the package creates in association with the price, marketing communications and branding.

- *quality*, which is the perceived and actual quality level of the component parts of the value offering. This includes the components used in the core product, along with the standard of the supplemental services or the supporting communications. Differentiation based on quality also drives the product's performance and brand reputation—for example, whilst low quality components are a tangible disadvantage, they will also lessen the conceptual advantage provided by the branding. Quality has the widest range of interactions with product differentiation as it operates through the full range of the relative competitive advantage spectrum.
- *sales effort*, which includes the abilities and capacities of the organisation's sales force (including their personal selling skills) and any exclusivity arrangements that can be made to block the sales of competitor products. It also covers the capacity of the salesforce to manage relationships with customers for the benefit of the organisation and its stakeholders.

As with the previous table, Table 11.3 examines the potential areas of interaction between marketing effort mechanisms and utility, value, relative advantage and the four levels of the product.

Product differentiation and the value chain

Product differentiation strategies will influence the operation of the value chain within the organisation. Whilst the value chain may be used initially to identify core competencies that can be used as areas of differentiation, it is also influenced by what is required of the organisation in creating, communicating and delivering the differentiated product. In summary, the primary value creation chain consists of the following interactions:

- *inbound logistics*, which is the process of managing the input flow of resources into the company. This aspect of the value chain has the greatest impact on, and is most influenced by, quality-based differentiation strategies. Raw materials brought into the firm need to be at the appropriate standard for the differentiated quality outcome. This aspect of the value chain may also influence product design if the differentiated feature set requires additional suppliers or source materials.
- *operations*, which is the process of turning the input into saleable value offerings for the customer. It impacts on the product design differentiation strategies, as this is the level of the organisation where the value offering is produced. Organisations with differentiation based on product design or quality need to develop core competencies at the operational level to achieve these outcomes. As noted in the previous chapter, operational costs can also influence the cost leadership strategies, and these in turn influence the pricing of the value offering.

TABLE 11.3 **Marketing effort mechanisms**

Differentiation	Perceived utility	Value proposition	Relative advantage	Product level
Branding	Personal benefit Quality	Perceived quality Organisational reputation Branding strategies	Intangible Conceptual	Augmented
Packaging	Performance Features	Functionality Branding	Tangible Conceptual	Augmented
Quality	Performance Service Quality	Functionality Quality Perceived quality Organisational reputation Intent to continue	Tangible Intangible Conceptual	Core Expected Augmented
Sales effort	Service	Organisational reputation Relationship Satisfaction	Intangible Conceptual	Augmented

- *outbound logistics*, which represents the assembly, processing, storing and shipping of the product to the consumer or the distribution channels, and covers the packaging and distribution differentiation strategies.
- *sales*, which represents the communication of the value offering to the customer and the value exchange process, and interacts directly with the sales-effort-based differentiation strategy. An organisation seeking to use a branding, marketing communication or sales effort will require a core competency in the primary chain aspect of sales, which can be supplemented with the secondary value chain aspect of marketing.
- *service*, which is the after-sales augmentation of the physical product's value offering, or the delivery of the service product's value. Consequently, this can influence the quality component of differentiation through marketing effort, and influences the product design of intangible value offerings.

Secondary value creation chains are those aspects of the organisation that do not directly contribute to the value offering, but represent the supporting elements of the organisation. Although these are not direct contributors to the value offering, they still have a role in product differentiation in the areas of:

- *procurement*, which is the process of acquiring the resources needed for each of the value-adding components of the value chain. This factor underpins the effective operation of the primary value chain, and whilst not influencing the eight mechanisms of differentiation specifically, its impact is felt through the level to which the primary value chain functions effectively.
- *technology development*, which is the process of ensuring that the technology used by the value addition processes has the best fit with the organisation. This can interact with the product and packaging design by ensuring the optimum level of technology and equipment is available to the organisation to implement differentiation in these areas.
- *human resources* refers to the capacity of the organisation to ensure the right sets of people, skills, abilities and motivation are available to the organisation as employees, contractors or other participants in the production process. This is most often seen as directly impacting on the sales effort, but also interacts with the product design, service quality and marketing communications differentiation elements.
- *systems*, which is the efficient and effective operation of the organisation through the management and control of organisational processes, systems and procedures. Differentiation based on quality will rely on organisational competencies in systems, with a focus on the need to develop organisation-wide quality control and total quality management processes. Systems may also impact on the capacity of the organisation to develop and implement differentiation through product design.
- *marketing*, which is the organisation's coordinated efforts to define 'value' in terms of how the customer perceives it, and creating a value offering that meets the customer's needs and wants. This area of the secondary chain is most obviously noticed through branding, sales efforts and marketing communication. However, as the whole of the product differentiation strategy is underpinned by the organisation's knowledge, understanding and involvement with the needs of the customer, marketing competencies with regard to market research are vital for success.

The primary interactions between the differentiation mechanisms and the value chain are summarised in Table 11.4.

Drivers of utility for the customer

The final step in the product differentiation process is to focus on the areas of utility for the consumer in order to create a differentiated value offering that meets the needs of the market. To recap, for the differentiated value offering to be perceived as valuable or relevant for the consumer, it must have the following features:

- *it must be real to the consumer*—the consumer must be able to perceive and receive the benefit offered by the firm.
- *it must be specific*—the differentiated advantage must be demonstrable to the consumer. General statements and promises of 'improvements' are not enough to generate utility or value.

TABLE 11.4 Differentiation and the value chain

Differentiation	Primary	Secondary
Marketing mix		
Price	Operations Sales	Marketing
Product design	Operations Inbound logistics	Technology development Systems
Marketing communications	Sales	Marketing
Distribution	Outbound logistics	Nil
Marketing efforts		
Branding	Sales	Marketing
Packaging	Outbound logistics	Technology development
Quality	Inbound logistics Operations Outbound logistics	Systems
Sales effort	Sales	Human resources Marketing

- *it must be able to be communicated and promoted*—a key element of being able to make the benefit real for the consumer. The organisation must know what benefit is being provided by the differentiation.
- *it must provide utility*—the differentiated product must live up to the communicated specific promised benefit, and that benefit must be useful to the consumer.

Utility has been examined in several forms in this chapter. As part of the product differentiation development process, the final variation on the concept of utility is the four subsets of utility derived from economics, and four drivers of utility as outlined by Doyle (2002).

Consumer-focused economic utility

Utility is a concept inherited from economics and is used to model the individual's perceived satisfaction arising from the ownership, use or consumption of the value offering (Doyle 2002). As an inherited theory, it has been adjusted and adapted in marketing to refer to quality, customer satisfaction or the level of needs fulfilment delivered by the product. There are four broad subcategories of utility:

- *form utility*, which is the utility derived from the production process combining raw materials and components parts into finished artefacts that are worth more than the sum of the component parts. For example, the form utility of a light bulb is

greater than the sum of the component parts of wires, glass and metal. Form utility underpins product design and quality in the differentiation mechanisms, and is interconnected to the inbound logistics and operations parts of the value chain.

- *time utility*, which is the value created by having a product available at the time the consumer desires it, and is interconnected with the distribution component of the differentiation mechanisms, and the outbound logistics of the value chain.
- *place utility*, which is the utility from having the product available where the consumer desires it. This interconnects with both time utility (having the product when and where desired) and the distribution aspect of the differentiation mechanisms. It also has two distinct interactions with the value chain—physical goods rely on the outbound logistics component, whereas services are also dependent on the operations and human resources components of the value chain.
- *possession utility*, which is the utility derived from having the legal right of ownership of the product, and the right to freely use it to meet the consumer's needs. It interacts with the quality and product design components of the mechanism of differentiation. As a consumer-centric function, it has limited involvement with the value chain, and is more closely associated with the relative competitive advantage concept.

The possible areas of interaction between these four components of consumer utility, and the previously covered areas of differentiation, perceived utility, value proposition, relative competitive advantage and the four levels of the product are examined in Table 11.5.

Doyle's drivers of utility

The final area of consumer-derived utility from differentiated products is referred to by Doyle (2002) as the drivers of utility, which represented four areas in which an organisation could enhance its value offering to the consumer. These four areas are:

- product drivers
- services drivers
- personnel drivers
- image drivers.

Product drivers

Product drivers are aspects of the physical goods or actual service that can be adjusted to the needs of the consumer. Adjustments to the product drivers will involve the primary value chain, with emphasis on the operation component. Similarly, altering these aspects of the value offering engages the product design aspects of the differentiation mechanisms. There are eight product drivers than can be altered to increase the perceived utility of the product. These are:

- *performance*—the core product offering, and the ability of the product to meet the basic needs of the consumer.

TABLE 11.5 Interactions of consumer utility

Type of utility	Differentiation	Perceived utility	Value proposition	Relative advantage	Product level
Form	Packaging Product design Quality	Performance Features Service Quality	Actual product Actual service	Tangible	Core Expected
Time	Distribution Sales effort	Availability	Actual product Actual service Relationship	Tangible Intangible	Expected Augmented
Place	Distribution Packaging Sales effort	Availability	Actual product Actual service Relationship	Tangible Intangible	Expected Augmented
Possession	Brand Marketing communications Quality	Personal benefit	Perceived image	Intangible Conceptual	Core Expected Augmented

- *features*—the expected product and augmented product levels of the components the consumer wants or expects to be part of the value offering.
- *reliability*—the inverse probability of the product encountering problems during normal use over its operational life span.
- *conformance to specifications*—the compliance of the value offering with specific market requests and customised needs.
- *durability*—the lifespan of the product, which is related to reliability and serviceability.
- *operating costs*—the anticipated addition costs of using the product. Reducing ongoing operating costs can be part of a cost leadership and pricing strategy for ancillary products related to the core product.
- *serviceability*—the extent to which the product can be repaired or have its durability extended through regular maintenance.
- *aesthetics*—the consumer's subjective opinion of the appearance of the product.

Table 11.6 summarises the interaction of these subcomponents with other aspects of the product differentiation process.

TABLE 11.6 **Product drivers and utility**

Product drivers	Differentiation	Perceived utility	Value proposition	Relative advantage	Type of utility	Product level
Performance	Product design	Personal benefit Performance	Actual product/ service	Tangible	Form	Core
Features	Packaging Product design	Performance Features Service	Actual product/ service	Tangible Intangible Conceptual	Form	Expected Augmented
Reliability	Product design Quality	Performance Features Service Quality	Actual product/ service	Tangible Intangible	Form Possession	Expected Augmented
Conformance	Product design	Performance Features	Actual product/ service	Tangible Intangible	Form	Expected
Durability	Packaging Product design Quality	Quality	Actual product/ service	Tangible	Possession	Expected
Operating costs	Price	Performance	Relationship	Intangible	Possession	Expected
Serviceability	Product design Quality	Quality	Relationship	Tangible	Possession	Augmented
Aesthetics	Brand Marketing communications Packaging Product design Quality	Personal benefit	Perceived image	Tangible Intangible Conceptual	Possession	Expected Augmented

Services drivers

Services drivers are part of the augmentation of physical goods, or the delivery of the service-based value offering. Altering the service drivers will involve the value chain elements of operations, human resources, service and sales effort. Service drivers are unique in that they represent the augmented product level for a physical good, and the core or expected products for a service-based value offering. Consequently, there is overlap between the product drivers and service drivers based on the tangibility of the original value offerings. However, the service drivers examined here are focused at the augmented product level. There are eight service drivers:

- *credit and finance*, which incorporates the range of alternative payment options an organisation can offer to the consumer. Differentiation based on this feature may also involve the organisation's creditor and financier stakeholders.

- *ordering facilities*, which are the mechanisms for taking the sale from the consumer, and which directly interact with the sales efforts of the primary value chain.
- *delivery*, which is the speed, accuracy and effectiveness of translating the consumer's order into the creation and delivery of the value offering. This covers outbound logistics, sales efforts and the organisation's relationship with the consumer.
- *installation*, which is the capacity to assist in the implementation of the value offering for the consumer.
- *training and consulting*, which includes the provision of additional post-sales assistance for the consumer to help with the use of the product or service.
- *after-sales service*, which is the quality of the post-transaction support for factors such as service or maintenance. This interconnects with the durability, reliability and serviceability of the product drivers.
- *guarantees*, which are any promises of the organisation as to the performance of its value offering in meeting the customer's needs.
- *operational support*, which is where the organisation offers additional services to assist the customer in minimising the cost of implementing the organisation's value offering.

The interaction and interconnection of these areas of augmented product differentiation are examined in Table 11.7.

Personnel drivers

Personnel drivers are the key attributes of the staff of the organisation, and how these skills and abilities can be used to position and differentiate the organisation's value offering. As personnel drivers are directly connected to the individual staff of the firm, product differentiation in this area has an impact on the employee stakeholder group, and directly influences the human resources requirements of the value chain. The eight differentiation points for personnel drivers are:

- *professionalism*, which is the extent to which the employees have the requisite training, and possess the requisite skills to deliver the service to the standard expected by the organisation and the consumer.
- *courtesy*, which is the treatment of the consumer by the employee.
- *trustworthiness*, which is the extent to which the consumer can rely on the honesty, integrity and credibility of the employee. Trustworthiness also interconnects with the relationship marketing aspects of the organisation's overall strategy, as consumers judge the organisation through the actions of the contact staff.
- *reliability*, which is the service consistency and the propensity of the employee to deliver quality service on time.
- *positiveness*, which is the external attitude of the employee, and the willingness of the employee to assist the customer in solving a problem.

TABLE 11.7 Interactions with the drivers of utility (1)

Service drivers	Differentiation	Perceived utility	Value proposition	Relative advantage	Type of utility	Product level
Credit and finance	Price Sales effort	Availability	Relationship	Intangible	Time Place	Augmented
Ordering facilities	Sales effort	Service	Relationship	Intangible	Time Place	Nil
Delivery	Distribution Packaging	Availability	Actual service Relationship	Intangible	Time Place Possession	Core
Installation	Distribution Product design Sales effort	Service	Actual service Relationship	Intangible	Time Place	Augmented
Training and consulting	Product design Quality Sales effort	Performance Features Service	Relationship	Intangible Conceptual	Possession	Augmented
After-sales service	Marketing communications Sales effort	Service	Actual service Relationship	Intangible	Possession	Expected Augmented
Guarantees	Brand Marketing communications Sales effort	Features	Relationship	Intangible	Possession	Expected Augmented
Operational support	Sales effort	Features Service	Actual service Relationship	Intangible	Possession	Expected Augmented

- *responsiveness*, which is the speed of response to the customer, including the speed of service delivery from the product drivers and service drivers.
- *initiative*, which is the freedom of the employee to be able to meet the customised needs of the customer within the frameworks set by the organisation to ensure the customer relationship is managed for the benefit of the organisation and its stakeholders.
- *communication*, which is the capacity of the employee to understand the needs of the customer, to communicate that information to the organisation, and to be able to be understood by the customer when communicating the organisation's message.

To a large extent, these eight factors each have a basic level that is part of the expected service. For example, customers would not expect unprofessional, unreliable or discourteous staff at a restaurant. In contrast, higher than expected levels of courtesy or professionalism would initially be a point of differentiation. However, these eight services drivers are also

TABLE 11.8 **Interactions with the drivers of utility (2)**

Personnel drivers	Differentiation	Perceived utility	Value proposition	Relative advantage	Type of utility	Product level
Professional	Brand	Service Quality	Perceived image Relationship	Intangible Conceptual	Nil	Expected Augmented
Courteous	Brand	Service Quality	Perceived image Relationship	Intangible Conceptual	Nil	Expected Augmented
Trustworthy	Brand	Service Quality	Perceived image Relationship	Intangible Conceptual	Nil	Expected Augmented
Reliable	Brand Marketing communications Sales effort	Service Quality	Perceived image Relationship	Intangible Conceptual	Nil	Expected Augmented
Positive	Sales effort	Service Quality	Perceived image Relationship	Intangible Conceptual	Nil	Expected Augmented
Responsive	Marketing communications Sales effort	Service Quality	Relationship	Intangible Conceptual	Nil	Expected Augmented
Uses initiative	Sales effort	Service Quality	Relationship	Intangible Conceptual	Nil	Expected Augmented
Communicates well	Sales effort	Service Quality	Relationship	Intangible Conceptual	Nil	Expected Augmented

relatively easy to copy and are prone to becoming part of the expected service. Consequently they should be used with restraint in efforts to differentiate the value offering. Table 11.8 overviews the service drivers of utility and their interaction with the differentiation process.

Image drivers

Image drivers are the intangible factors associated with the organisation, and the socio-psychological confidence that these factors give a consumer about using the product associated with this brand. These are:

- *reality*, which is the organisation's actual reputation in the marketplace as a result of the performance of its value offerings, and its position in the minds of the consumer as result of prior marketing messages.
- *marketing communications*, which are the deliberate and constructed marketing messages used to position and differentiate the value offering.
- *branding*, which is the inherent value of the brand as a mental shortcut to indicate quality, social prestige and the utility value of the product.

The interaction of image drivers with the differentiation process is examined in Table 11.9.

TABLE 11.9 **Interactions with the drivers of utility (3)**

Image drivers	Differentiation	Perceived utility	Value proposition	Relative advantage	Type of utility	Product level
Reality	Brand Packaging Price Product design Quality	Personal benefit Performance Features Service Quality Availability	Actual product Actual service Relationship	Tangible Intangible	Form Time Place Possession	Core Expected Augmented Potential
Marketing communications	Brand Marketing communications Packaging Sales effort	Quality	Perceived image Relationship	Conceptual	Form Possession	Core Augmented Potential
Branding	Brand Marketing communications Packaging Quality	Personal benefit Quality	Perceived image	Conceptual	Possession	Augmented

Conclusion

Product differentiation allows the organisation to develop a unique position in the market based on the overall value offering it provides to its target market. However the key to successful differentiation strategies lies not in the technical differences in the product offering, but rather in how these differences are perceived by the market. Over time there have been numerous examples of a 'superior' product failing in the market while an 'inferior' product became the market leader. In all cases, the reason for this is that the features valued by the organisation in its product-focused philosophy, failed to add perceived value to its customers. Following a product differentiation strategy requires a true adoption of the full marketing concept and philosophy.

Understanding customer needs, what constitutes 'value' in the market and communicating this underpins the success of the strategy. Value can be derived from the physical features of the product or from intangible and conceptual features such as the social status acquired as a result of owning or using the product, or the ease of use of the product. Regardless of the basis used in developing the point of perceived differentiation, such a strategy can only succeed if the differentiation can be effectively communicated to the market and is considered to be both unique and valuable.

Value addition and strategic competitive advantage 3—Niche strategy

CHAPTER 12

Introduction

Niche strategy is based on the idea of identifying a small segment of a broader market, and becoming the market leader within that narrowly defined group of consumers. This business approach relies on the close match between the strengths of the organisation and the needs of a narrowly defined market. Rather than trying to appeal to a wide range of consumers, the niche strategy selects more specialist needs on the assumption that the niche can be served profitably as customers will pay more for a product that meets a unique need. This chapter examines how to implement a niche strategy, types of niche markets, and how to integrate the knowledge from the internal and external analysis chapters to identify and target possible niche market strategies.

Defining niche strategies

Unlike previous marketing strategies, niche strategy does not have a consistent set of definitions. The following list outlines six definitions of niche strategy from six different authors. These are:

- small sub-segments of the market with distinct needs (Wood 2004)
- small markets consisting of individual or small groups of customers with similar characteristics and needs (Dalgic & Leeuw 1994)
- the process of carving out small markets of unmet needs (Shani & Chalasani 1992)
- market segments within market segments (Best 2005)
- discrete market segments (Viljoen & Dann 2003)
- specialisation in a single market (McDonald & Roberts 1992).

For the purpose of this chapter, a new definition of niche strategy, based on the common grounds of the six definitions cited is defined as:

> the type of business strategy that focuses the organisation on creating, communicating and delivering a value offering to a small, discrete market segment of individuals or groups who have specific unmet needs that are distinct from the rest of the market segment.

In this context, niche strategy is using the Best (2005) 'market within a market' focus. However, this is not universal in niche marketing strategy, and other authors and texts will differ in their definition of niche strategies.

To add to the complication of the definition of niche marketing, there are also five modes of niche strategy that need to be considered based on the existence of the niche, the value offering or whether a new niche or new product is being proposed. Table 12.1 outlines the 2 × 2 matrix of niche marketing which paradoxically contains five alternative strategies.

TABLE 12.1 Types of niche market

	New product	**Existing product**
New niche market	**Entry niche (1)** *New product* *New niche market*	**Extra-niche segmentation (2)** *New niche market* *Existing product*
Existing niche market	**Intra-niche (3)** *New product* *Existing niche market*	**Focus niche (4)** **Exit niche (5)** *Existing niche market* *Existing product*

Table 12.1 results in the following types of niche strategies:

1. *entry niche (new product, new niche)*, which is where the niche strategy is used to introduce a new product to a new niche, either through diversification or new-to-the-world products that create niche markets.
2. *extra-niche segmentation (new niche, existing product)*, which is the use of market development to create a niche based on the use of an existing product, or the use of

marketing segmentation to identify new users of the existing product as a new segment, this includes segments that arise from use innovations.

3. *intra-niche (new product, existing niche)*, which is where members of the market niche create products to service the needs of niche peers, or where an organisation enters a niche as part of a product development strategy.
4. *focus niche (existing niche, existing product)*, which is where the organisation servicing an existing niche uses market penetration strategies to increase its sales volume to the niche.
5. *exit niche (declining existing niche, existing product)*, which is a form of defensive marketing and exit strategy where the organisation consistently reduces the focus of its operations until it reaches a sustainable niche while exiting the marketplace. This will be examined in further detail in Chapter 13.

Niche strategies can draw on other marketing strategies, and may be used as part of a combined strategic implementation. For example, market penetration (Chapter 7) is part of the focus niche strategy, and product development (Chapter 9) underpins the entry niche and extra-niche strategies.

Assumptions of niche strategy

Niche strategy is dependent on a range of assumptions for its operation, and is also subject to the assumptions of any companion strategy, e.g. market penetration. Consequently, niche strategy is akin to a micro-level marketing strategy where all of the basic assumptions of marketing strategy are present. However, the assumptions which are most generic in niche marketing are:

- *niche markets can be identified by segmentation criteria*, which is the belief that the niche segment can be separable, discrete, distinguishable and will respond to the organisation's offering.
- *a narrow target segment can be created through markets which can be further reduced by segmentation*, which is an inherent assumption of this strategy that the broader market contains a series of sub-market niches. This underpins the entry niche and extra-niche segment strategies, and is related to the market development strategy (Chapter 8) and diversification strategy (Chapter 2).
- *a narrow targeted segment already exists*, which underpins the intra-niche and focus niche strategies. This is also related to the assumptions that underpin market penetration (Chapter 7) product development (Chapter 9) and product differentiation (Chapter 10).
- *an existing value offering*, which is assumed by segmentation and focus niche strategies. This also relates to the assumptions inherent in market penetration (Chapter 7), market development (Chapter 8) and product differentiation (Chapter 10).

In many respects, product differentiation and niche marketing share the most common ground between the growth and value addition strategies. However, as mentioned previously, niche marketing focuses on value offerings for a narrow market segment. In contrast, product differentiation is aimed at positioning the value offering as a unique product within wider market segments or the broader industry.

Market segmentation and niche strategy

Within niche strategy, there are assumed preconditions of marketing segments, either through the external focus of an organisation on dividing a market into niches, or from the intra-niche expansion of product users from individual adopters to a market niche. Consequently, segmentation is briefly recapped before being applied to niche strategy. Woods (2004) outlined a three-step top-down process for market segmentation which can result in the identification of market niches:

- choose a market
- apply a segmentation variable
- evaluate and select a segment (Chapter 6).

Each approach to niche strategy uses a subtly different variation on the Wood (2004) market segmentation theory. These are outlined in Table 12.2.

TABLE 12.2 Segmentation by niche sub-strategy

	Niche entry	Extra-niche	Focus niche	Intra-niche
Choose a market	Find gap/create new market niche	Select new or existing market	Select current niche	Identify current niche membership
Apply segmentation variable	Willingness to adopt new product/ innovators	Unmet need in the niche for the existing product from another niche	Needs currently being met by existing product	Unmet need in the niche that can be served by niche product
Evaluate and select a segment	Will adopt the new to world product	Will adopt new to niche product	Will purchase current product again/in greater volume	Is current member of niche who will adopt the product

Key elements of market segments

As niche strategy has a dependence on marketing segmentation theory, Kotler's (1998) checklist for market segmentation (Chapters 6 and 8) is repeated here. The five key questions to answer are:

- Is the niche homogenous?
- Is the niche heterogenous?
- Is the niche clearly identifiable?
- Is the niche measurable and substantial?
- Is the niche accessible and sustainable?

In addition, niche strategies have the following generic requirements that the niche markets need to fulfil. These are:

- *the niche market is small*, which is the differentiating factor between niche and segmentation. This is possibly the only universally supported proposition in niche strategy literature (Shani & Chalasani 1992; Dalgic & Leeuw 1994; Viljoen & Dann 2003; Wood 2004; Best 2005) although there is no parameter set to determine what 'small' means at the operational level.
- *the organisation can produce a competitive advantage within the narrow market*, which is the capacity of the organisation to either differentiate the product offering to the niche (Chapter 11) or to dominate the market through a superior value offering (Dalgic & Leeuw 1994).
- *there is cyclical stability within the market, or the market can be sustained over time*, which is the level of ongoing viability of the market, and is closely associated with the market attractiveness of the niche (Chapter 2 and 5). This is independent of the sustainability of the organisation's venture into the market which is tied to cost leadership (Chapter 10) and the value chain (Chapter 5).

Tactical value of niche strategy

Niche strategy is a micro-implementation of broader business strategy. As such, it has the tactical value, advantage and disadvantage of the general business strategy. In general, much of the benefit of niche strategy is derived from it being the combined application of segmentation (Chapter 6), product differentiation (Chapter 10), cost leadership (Chapter 9) and market development (Chapter 8). Consequently, the tactical value of niche strategy should be considered as the sum of the broader business strategies it encompasses, and the specific benefits from the use of the appropriate sub-components. These are:

- *entry niche strategies*, which have the inherent value of being the first market in which the organisation attempts to recoup its research and development costs. Organisations using the entry niche approach target the innovator niche of their broader market segments with the intention of expanding beyond the initial niche into early adopters and the broader market through market development (Chapter 8).
- *extra-niche strategies*, where the value of the strategy is through the application of market development in niche-by-niche growth strategy. It can also be used to assist the movement of an entry-niche innovation into the broader market. Further,

the extra-niche approach allows the organisation to capture a larger market in a series of smaller campaigns and investments over time, which can be used to minimise head-to-head challenges with market competitors.

- *intra-niche strategies*, which derive their value in serving an existing niche market through delivering a new value offering for that market (Chapter 9).
- *focus niche strategy*, which is the application of market penetration strategy to assist the organisation to dominate the specific market niche. In addition, this can be used as a defensive strategy (Chapter 13) or as a mechanism to raise the barriers to entry (Chapter 5) in the niche market.
- *exit niche*, which is an applied defensive marketing exit strategy where the organisation reduces the focus of their operations until they reach a sustainable niche and/or they exit the marketplace.

Core principles of niche strategy

The principles of implementing a niche strategy are based around three broad areas, which are:

- *the steps to implement a niche strategy*, which is the generic level approach that can be tailored for use with each type of niche sub-strategy
- *the types of niche markets*, which examines different characteristics of niche market types
- *the duration of a niche strategy*, which is the length of time an organisation can expect to spend using a niche strategy, and depends on the purpose of the niche approach and which of the four methods was selected.

Steps to implementing a niche strategy

The nature of the niche strategy as a microcosm of the larger competitive market strategy set is that it can be presented as a generic process which is adapted to the implementation of one of the sub-niche approaches. Dalgic and Leeuw (1994) outline a series of steps for developing and implementing a niche strategy:

- gain organisational insight
- gain customer insight
- gain competitor insight
- develop a continuous information system to maintain awareness of the market
- apply differentiation strategy
- focus organisational effort and product lines
- raise market barriers to competitor entry to the niche
- limit and focus market commitments by restricting growth and number of niches
- adhere to a corporate strategy
- ensure minimum levels of diversification.

Organisational insight: internal analysis

Internal analysis is the process of understanding the organisation in terms of the business's strengths and weakness, core competencies and competitive position in the niche market. Consequently, this first step draws heavily on the existing information collected by the organisation in the internal analysis (Chapter 4) and makes use of analysis models such as the Directional Policy Matrix (Chapter 2) and the value chain (Chapter 4). Internal analysis of the organisation should also address any potential production context stakeholder issues that might arise from a niche strategy selection. In addition, the internal analysis should examine the value chain for areas of core competency that could be used for:

- differentiating the niche value offering (Chapter 11)
- forming the basis of a new or improved offering to a new or existing niche (Chapters 8, 9 and 10)
- developing cost leadership for the current niche product (Chapter 10).

Customer insight: internal and external analysis

The second step of the process is the organisation's investigation and understanding of the needs of the target niche. Customer analysis forms the core of most marketing strategy, and niche marketing is heavily dependent on an intimate understanding of a small number of customers. This section draws on multiple areas of previous analysis, including internal (Chapter 4) and external analysis (Chapter 5), the customer stakeholder analysis (Chapter 3) and the organisation's objectives (Chapter 6).

As the core definition of marketing depends on the management of the relationship with the consumer for the benefit of the organisation and its stakeholders, the 'gain customer insight' step needs to examine the current relationships with niche customers through core customer outcomes (Chapter 4). This should also be undertaken for potential new customers in the customer analysis (Chapter 5) for the overall purposes of assessing if new or continued involvement in the relationship with the niche will benefit the organisation.

Customer analysis for niche strategy should make specific use of the Kano Method (Chapter 5) for determining the core, expected and augmented levels of the niche value offering. The feature set outlined by the Kano Method includes:

- *one-dimensional features*, which determines the satisfaction of the niche, and which would be expected to be the core product (Chapter 11)
- *must be features*, which are simply assumed to be present by the niche and form the expected product (Chapter 11)
- *attractive features*, which form the augmented product by improving the satisfaction experienced by the niche when the features are present (Chapter 11)
- *reverse features*, which are those features that the niche does not need or want. Removing these features from a value offering may form the basis of a differentiation strategy based on the improved utility of the product for the market niche
- *indifferent features*, which are those features that the customer does not care about, and which can be removed without the customer noticing.

Competitor insight

The third step in the process is to make use of the competitor analysis (Chapter 5). In niche strategy development, competitor analysis may be used to determine if the mere presence of an existing rival value offering is a sufficient market barrier to make the niche less than viable. Customer analysis in this stage also provides the basis for determining the relative competitive advantage of the organisation's value offering against any potential competitors. Similarly, knowledge gained in Porter's industry analysis (Chapter 5), Five Forces analysis (Chapter 2) and the competitor analysis (Chapter 5) can be applied to the competitor insight stage. Organisations planning a niche strategy need to undertake Lehmann and Winer's (1991) four-step model (Chapter 5). These steps are:

- assess the current and future objectives of the competitor
- assess the current strategy of the competitor
- assess the resources available to the competitor
- predict the future strategies of the competitors.

Organisations assessing new niches, or niches based on new products, need to assess potential competitors to these markets. The attractiveness of a niche to the organisation may also make it an attractive target to competitors, particularly where the organisation is planning either an extra-niche segmentation of an existing market with existing competitors, or during the focused niche exit strategy.

Develop a continuous information system

The fourth step in the process requires the establishment and ongoing use of systems of information management. Information management systems interconnect the systems element of the secondary value chain components (Chapter 5) with the external analysis elements of competitor analysis and industry analysis (Chapter 5). Niche strategies based on differentiated value offerings and relative competitive advantages need constant monitoring to ensure that the differentiated factor of an augmented product does not shift to become part of the expected product. When that occurs, the feature is no longer a source of differentiation for the firm. Similarly, monitoring the broader competitive market segments can aid in defending a market niche by being aware of the actions of larger competitors in related market segments. This step amalgamates three individual elements of Dalgic and Leeuw's (1994) process. The original steps were:

- develop a continuous information system
- maintain awareness of the market
- maintain constant development and adjustments.

Merging these three elements provides a purpose and outcome for the continuous information system to be driven by market awareness and to feed into constant development and adjustment of the value offering.

Apply differentiation strategy

Niche segments and strategies require the organisation to offer something of unique value to a small market, which in turn depends on the value offering being able to differentiate itself. Consequently, the theory and practice of product differentiation in Chapter 10 will assist the organisation with the extra-niche, intra-niche and focus strategies. However, as differentiation is precluded from applying to diversification strategies, it cannot be applied to the entry niche strategy for similar reasons. However, entry niche strategies create their own form of unique positioning by being innovations, targeted to the innovator or early adopter niches, and providing unique value offerings that are independent of a differentiation strategy.

Focused organisational effort and product lines

This step in the process is a reminder for the organisation that is operating multiple value offerings in multiple markets to maintain an overarching control (Chapter 15) to ensure that market cannibalisation does not occur, and that the organisation does not compete against its own value offerings. Rather, product line extensions, ancillary products and related value offerings should be coordinated to deliver complementary coverage of the needs of the niche market.

Raise market barriers to competitor entry to the niche

Whilst most of the mentions of barriers to the market in the context of strategy have been designed to assist the organisation to enter a blocked market, the purpose of the niche strategy is to dominate and control a single segment. To do this, the organisation has to defend its market by creating barriers to competitor's entry through actions such as:

- *exclusivity arrangements*, which can be made with suppliers and distributors in order to encircle a market (Chapter 6).
- *relationship marketing*, which covers any attempt to lock in long-term contracts, and relationships with high-value customers. This also covers developing co-creation systems such as just-in-time delivery and other forms of co-dependence between customer and organisation in order to increase switching costs for the customer, and decrease the opportunities for late-arriving competitors.
- *social expectations*, which is where membership of the niche becomes associated with the social message presented by the organisation's product, and switching to a competitor's offering would risk the consumer's place in the social group.
- *technical, legal and patent barriers*, which is where the organisation blocks new competitors through non-marketing techniques such as patents on key elements of the value delivery process.

Limit and focus market commitments

Niche marketing strategies can distract an organisation as it attempts to gain market share by moving from niche to niche and by progressively spreading its resources more thinly. The purpose of this step is to maintain the narrow focus of the organisational objectives that led to the niche strategy being selected in the first instance—that is, the intention to dominate a

tightly defined segment of the market. This ties into the financial objectives of the organisation, along with the stakeholder groups of the financiers, creditors and shareholders.

Adhere to a corporate strategy

This step is related to the organisational focus and market commitment, however this is specifically aimed at maintaining an organisational agenda by staying in line with the overall corporate strategy. This relates to the corporate strategy step in the model of new product development (Chapter 9) in that the niche strategies need to fit into the overall goals and objectives of the organisation.

Ensure a minimum level of diversification to avoid dependence on a single product or market

The final step in the niche strategy process is to attempt some level of diversification to ensure that wherever possible, the organisation is not reliant on a single value offering to a single niche market for its long-term survival. The objective of any organisation should be to build a sufficiently sustainable niche, customer and product portfolio to ensure its long-term survival.

Types of niche markets

Niche strategies create different forms of market niches, which can be grouped together under three different categories for examination. These three groups are:

- product differentiation niche strategies, which include:
  - specialist product niches (Cohen 2001)
  - specialist skill provision (Cohen 2001)
  - price niche (Falkenstein 1996)
  - personality niche (Falkenstein 1996).
- Direction policy matrix niches, which include:
  - toll gate (Cohen 2001; Shani & Chalasani 1992)
  - growth niche (Best 2005; Doyle 2002; Hussey 1978)
  - exit niche (Doyle 2002; Hussey 1978).
- analysis-derived niches, which include:
  - specialist customer requirements (Shani & Chalasani 1992)
  - specialist market demand (Cohen 2001; Falkenstein 1996)
  - use innovation niche (Falkenstein 1996; Shani & Chalasani 1992).

Product differentiation niche strategies

Product differentiation niches are those markets that are built around the usage of the product, rather than an independent segmentation variable such as psychographic profile or geographic location. These forms of niche markets draw heavily on the product differentiation strategy (Chapter 11) and on cost leadership theory (Chapter 9). Four types of product differentiation market are identified:

- *specialist product niches* that form around the use of an innovation or specialised value offering from the firm. These types of products can be identified and enhanced

through value proposition analysis (Chapter 4), or utility analysis methods (Chapter 11) of product differentiation. Niches based around specialist products have two major risks—first, that the niche itself may not be sustainable in the long term without expanding into accompanying market segments, and second, that the expansion into the new segments may require alteration of the value offering, thus reducing its specialist value. Alternatively, specialist niches may arise from an exit niche which regains momentum—for example, vinyl albums and turntables became an exit niche for many organisations until the specialist product requirements of the DJ niche market were addressed, and created a profit-producing niche.

- *specialist skill provision*, which is the service industry equivalent of specialist product niche. Specialist skills can be the core product, e.g. specialist repair skills or consultancy abilities, or they may be part of the service drivers of training, after-sales service or guarantees to a core product. In either case, specialist skill niche markets are heavily dependent on the skill set of the employee, and as such, are vulnerable to the personnel driver issues (Chapter 11), human resource issues (value chain) and the employee stakeholder issues (Chapter 3). Specific areas of concern arise where specialist skills have formed from a declining market, or from a revived exit market niche. For example, the skill sets associated with blacksmiths and farriers create a niche market for the output product, and a smaller niche for their services, which is progressively less attractive to new employees. Organisations with niches based on specialist skills need to be aware of the ageing of their labour force and either train new employees or consider the skill-based niche to be a limited-term market opportunity.
- *price niche*, which is where the organisation creates a niche market based around delivering the value offering for either a market-leader low price or prestige-inducing high price. Price niche markets are the most volatile, highest risk and least unique markets for an organisation to use as a niching strategy. Low-cost niche approaches rely on cost leadership for the survival of the niche, and also depend on highly efficient and tightly controlled value chains. At the opposite extreme of the price niche, prestige price-based niches require the quality management of the value chain to ensure the product satisfies the expectation of the consumer who paid a premium for its ownership. Premium-price niches are closely interconnected with personality niches, although a personality niche does not require a premium pricing strategy.
- *personality niche*, which is where the niche is based on association with the organisation and the value offering's brand personality. Brand personality is the unique set of social benefits that are conveyed by association with the organisation through the use of its products, and may be used to form niche brand communities. One of the most heavily cited examples of the personality niche is the Harley-Davidson brand, which extends a personality niche across a range of products from the core business of motorcycles through to extended options of fashion accessories and giftware. Similarly, sports teams, musicians, bands and even computer games

can generate personality-based niches where they hold a relative conceptual advantage over any other entrant into the niche area. Further, as utility is derived from association with the branding and marketing communication of the organisation, this raises the barrier to entry for rival competitors. Whilst they can create their own personality, they cannot copy the unique feature set of the personality of the niche. The risk inherent with a personality-driven niche is a change in fashion, or for the personality to lose its appeal through controversy or other events. Utility of the personality niche is derived from the intangible and conceptual benefits which are difficult to replace or repair when damaged through scandal, overexposure and brand burn-out.

Table 12.3 covers the interaction between the four differentiation niches and related strategy theory covered elsewhere in the book.

TABLE 12.3 Niche differentiation

Type of niche	Dominant niche strategy	Related theory	Primary value chain	Secondary chain
Specialist product	Extra-niche Focus niche	Product differentiation	Operations Inbound logistics	Technology development
Specialist skill provision	Extra-niche Focus niche	Product design	Inbound logistics Operations Service	Technology development Human resources
Price	Extra-niche Exit niche	Cost leadership	Operations Sales	Systems Marketing
Personality	Focus niche	Branding/ marketing communication	Sales	Marketing

Directional policy matrix niches

Direction policy niches are niche markets that arise as a result of the organisation using a Directional Policy Matrix to determine its niche business strategy. Hussey (1978) outlined the Shell Chemical Directional Policy Matrix, which used a 3 × 3 grid of market attractiveness and business strength to determine strategy (Chapter 2). The directional matrix elements of leader, growth leader and two forms of phased withdrawal can generate specific market niches:

- *toll gate*, where the organisation dominants a niche by providing a value offering that is essential to the market. This requires the organisation to develop a product with sufficient niche appeal, either through conceptual or tangible relative

advantage, that non-use of the product is more expensive financially or socially than the financial price of the product. Toll gate niches create strong relative competitive advantage positions for the leading organisation which, by dominating the niche, also gains a high level of industry attractiveness from the niche. Consequently, this style of niche market is closest to the leader element of the Directional Policy Matrix.

- *growth*, where the niche develops in a growing market and is either created by the introduction of the product (Chapter 9), market development (Chapter 8) or diversification (Chapter 6) led by really new products (Chapters 2 and 9). In all three cases, this is best represented by the growth leader position in the Directional Policy Matrix. Growth niches are often intermediate positions between larger market segments and the development of a differentiation niche strategy.
- *exit*, which involves the phased withdrawal of a product from a wider market segment to a smaller less price-sensitive niche of consumers. Exit niches are often temporary positions that result in following the Directional Policy Matrix to full market withdrawal, or that can be converted into focus niches through market penetration.

Table 12.4 outlines the crossover between these three types of niches and the existing strategy theory and practice covered in this text.

TABLE 12.4 Policy direction matrix niche

Niche strategy type	Niche strategy	Related theory	Primary value chain	Secondary chain
Toll gate	Focus niche Intra-niche	Relative competitive advantage	Operations Outbound logistics Sales	Marketing
Growth	Entry niche Extra-niche Intra-niche	Growth leader New product development Diversification	Inbound logistics Operations Outbound logistics Sales	Marketing
Exit	Divest	Phased withdrawal	Operations Sales	Systems Marketing

Analysis-derived niches

The niche markets in the third group are identified by their interaction with the organisation's internal and external analysis processes. These types of niches can be driven by

extra-niche or segmentation strategies that are designed to find problems to match the organisation's currently offered solutions. However, the analysis approach may also be used to examine the current niche for opportunities for product development and utility enhancement. The analysis-derived niches include:

- *specialist customer requirements*, where the niche strategy arises from the needs of the customer being communicated through the customer relationship, and the organisation responding with a specific niche offering to meet these needs. This niche approach can incorporate product differentiation (Chapter 9), cost leadership (Chapter 10), product development (Chapter 8) and market penetration (Chapter 9). Specialist customer requirement strategies also interact with other aspects of the organisation's business activities (such as the development of just-in-time delivery, customer co-creation and order-routine specification—Chapter 5). This impacts on the primary value chain elements of the operations and outbound logistics where the requirements lead to custom product processes.
- *specialist market demand*, where the organisation targets a known niche to look for areas where new product development could be used to meet specific market needs. This interconnects with the external analysis (Chapter 5), product differentiation with specific regard to unmet utility drivers or unsatisfactory core product offerings (Chapter 11). Specific market demand can also arise from within the niche or from the organisation creating a product to solve its own need, which in turn can then be on-sold to a niche market. For example, during the value chain analysis, the organisation may develop a customised machining process for packaging. This packaging process could then be sold or licensed as a niche product to other organisations with similar market needs.
- *use innovation*, where use innovations are derived from the original market, and developed into specific niche value offerings through the use of the lead user analysis and the Kano Method (Chapter 5). Niches whose creation is based on lead user analysis are often temporary phases as the organisation attempts to develop them into toll gate, personality or specialist product niches.

Table 12.5 examines how these three niche markets interconnect and interact with the other activities of the organisation.

Types of niche duration

One area of commonality between the niche market and broader market segmentation is the uncertain duration of the market's lifespan. Niche markets are prone to faster product life cycle curves (Chapter 2) due to their smaller size and specifically targeted value offerings. Doyle (2002) outlined the niche market as a short-term temporary measure where the organisation seeks to expand the niche into a broader, less vulnerable market segment. Dalgic and Leeuw (1994) contradict this strategy with the suggestion that niches based on relationship marketing can be translated into long-term viable markets. On review, niche strategies can lead to a range of niche durations based on the purpose of the niche, the

TABLE 12.5 Analysis derived niche

Niche strategy type	Niche strategy	Related theory	Primary value chain	Secondary chain
Specialist customer requirements	Niche entry Extra-niche Intra-niche	Core customer outcomes Relative competitive advantage New product development Market development Product differentiation	Inbound logistics Operations Outbound logistics Service	Technology development Human resources Systems
Specialist market demand	Niche entry Extra-niche Intra-niche	Customer analysis Utility drivers	Inbound logistics Operations	Technology development Marketing
Use innovation	Niche entry Extra-niche	Lead user analysis	Operations Sales	Marketing

nature of the value offering and the objectives of the organisation. Common niche time frames include:

- *short-term positive transition niches*, which are those niche markets which are transitionary phases such as the growth niche, or the niches of innovators and early adopters of new products. These types of markets are also connected to the question marks of the BCG Matrix, and usually represent a high-growth market.
- *short-term negative transition niches*, which include those niches that arise as an organisation scales back its product lines and value offerings and prepares to withdraw from the broader marketplace (as occurs with the exit niche). This is usually the result of a previous market segment being identified as a 'dog' in the BCG Matrix, or being part of the phased withdrawal element of the Directional Policy Matrix.
- *medium-term exploitation niches*, which encompass a mid-level of sustainability, but which are not expected to continue as independent market segments. For example, product differentiation niches are usually based on medium-term strategies as the organisation expects the points of differentiation to be duplicated by competitors or become part of the expected product, thus negating their niche

utility value. Medium-term exploitation niches are associated with the cash cows of the BCG Matrix and the cash generation strategies of the niches.

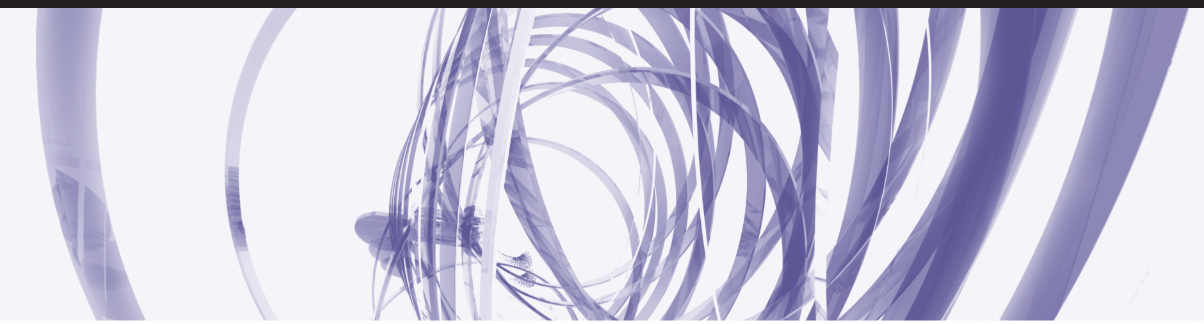
- *medium-term toll gate niches*, which is where the organisation has plans to develop the dominated niche through market penetration, and to use it as a core revenue stream whilst expanding into other market niches through market development. These types of niches are most closely associated with the BCG Matrix question marks and the 'proceed with care' or 'double or quit' elements of the niches. Medium-term toll gates can also be used as a basis for product differentiation into other niches through use innovations or new product development.
- *long-term relationship niches*, which is where the organisation and the niche customer are interconnected through just-in-time product, customised product solutions or the use of the personality niche. This incorporates the specialist skill, consumer requirements, product and demand niches approaches where they lead to an ongoing marketing relationship between the organisation and members of the niche.

Conclusion

Niche strategies are a distinct form of the business strategy that focuses the organisation's operations on a narrow band of customer's needs. This involves creating, communicating and delivering a specific value offering to a small, discrete market segment with specific unmet needs that are distinct from the rest of the market segment. This chapter has overviewed the core principles of niche strategy, including the steps required to effectively implement a niche approach to business, and the types of niche markets likely to be encountered by the organisation. Finally, the chapter examined the variable duration of the niche strategy, from the short-term transitionary approach, through to the long-term focus of the niche domination strategies.

Defensive marketing—Maintaining the position

CHAPTER 13



Introduction

This chapter covers five approaches to defensive marketing strategy including leadership, maintenance, niche, harvest and divesting strategies. Leadership strategies involve the domination of the declining market to secure the long term survival of the organisation and the market place. Maintenance strategies are those strategies that are used to fortify the current market positions. Harvest strategies address the situation where the organisation engages in medium term planned strategic withdrawal from a market. Niche strategy narrows the organisational focus to serve smaller, less price sensitive markets. Finally, divesting strategies are where the organisation either sells its interest in its value offering to a competitor or ceases trading in the market.

Assumptions of defensive marketing strategy

Two core principles underpin defensive marketing strategy. First, there is an assumption that the organisation can, and will, divest itself of unprofitable customers or markets. Being

willing to ‘sack’ unprofitable customers to maximise returns to the firm emphasises the inherent conflict in the 2004 definition of marketing between ‘managing customer relationships in ways that benefit the organisation and its stakeholders’ and ‘creating, communicating and delivering value to customers’. In essence, the organisation can only focus on the creation, communication and delivery aspect until the point at which it becomes detrimental to the organisation. At that point, the organisation either has to revitalise the value offering so that it becomes beneficial again or divest itself of the relationship with the customer.

Second, defensive marketing assumes that the product or value offering under consideration can be removed from the organisation's value offerings. This assumption becomes more important in divesting strategies, although it also plays a role in determining whether the organisation can remove product or brands from the market without compromising the long-term success of the organisation or its reputation. Where the organisation has its identity closely associated with the brand or product, it may need to continue producing this value offering at a loss that is sustained and cross-funded by other products as part of the ongoing branding and image of the firm. For example, if Harley-Davidson decided to divest itself of the motorcycle line because it was unprofitable, even if the rest of the Harley-Davidson product lines were currently profitable, the loss of the key product that creates the brand identity would devalue the whole of the company.

Tactical value of defensive marketing strategy

Defensive marketing strategy has a relatively simple tactical value and, consistent with the truism that the shorter sections in the text are the longest processes for the organisation in practice, it also has one of the most vital roles to play in the survival of the organisation. Defensive marketing strategies can be used in three ways:

1. *to protect and consolidate market share*, which is where the maintenance strategy is used ahead of a growth outcome. Maintaining existing customers, and ensuring an ongoing revenue stream from a core of satisfied customers, is essential for the long-term survival of an organisation.
2. *to maximise cash flow and per-unit revenue in maturing markets*, which is where the harvest strategy is used to provide the organisation with an increased cash flow to use to cross-fund future-focused portfolios (Chapter 4), increase shareholder value (Chapters 3 and 4) and act as cash cows for the organisation (Chapter 2).
3. *to reduce liabilities and non-contributing business functions,* which is where aspects of the organisation's value offerings which do not contribute to the overall success of the firm are shut down or sold off. Loss-making areas which either provide relative conceptual advantage or which create the market for other organisational products (e.g. printers which drive demand for toner cartridges) should not be subject to divestment.

In general, defensive marketing strategies provide a mechanism for the organisation to secure the value offering against unrealistic expectations of perpetual growth (maintenance),

the organisation against potentially loss-making ventures (divestment), and to generate cash flow from existing markets (harvest and maintenance).

Defensive marketing strategy

The core elements to understand about defensive marketing strategy include:

- types of defence
- types of defensive marketing strategies
- defensive market leadership
- risks of defensive market leadership
- defensive maintenance strategy
- defensive niche strategy
- defensive harvest strategy
- defensive divestment strategy.

Types of defence

Before outlining types of defence, it is important to review the six types of confrontational methods (Chapter 6). These methods were:

- *frontal attack*, where the organisation takes an all-out offensive against a specific market or organisation
- *flanking attack*, where the organisation sets its strength against the competitor's perceived or actual weakness
- *encirclement attack*, where the organisation tries to cut off its rival's supply and/or distribution channels
- *by-pass strategy*, where the organisation changes the rules of engagement without competing directly with the existing product suppliers
- *guerrilla tactics*, where the conventional strategies are set aside in favour of subtle, underground marketing efforts either to raid market share or gain trial adoption by consumers of an existing product
- *non-confrontational tactics*, where the organisation focuses on its own customers, markets, value offering and value chains without directly launching an offensive on its market competitors.

Hooley, Saunders and Piercy (2004) outline defensive strategies that can be used to form the basis for a defensive marketing strategy to counter the previously listed methods of attack. The six defensive strategies are:

- *fortification*, which is a proactive defence where the organisation concentrates on improving its relationship with the existing market, and raises barriers to market entry. These barriers can include strong product differentiation, branding, relative competitive advantage (Chapter 11) and the creation of personality niches (Chapter 12). Fortification strategies can also be used in conjunction with niche

strategies (Chapter 12) to dominate an area of the market or as part of a market penetration approach to secure ongoing customer retention (Chapter 7).

- *flanking defence*, which is where the organisation blocks a competitor's attempted flanking attack by increasing its strengths on its 'flank' products and weaker areas. This is a reactive strategy that has two major risks associated with its use. First, drawing resources to the weaker flanks may deplete the stronger areas of the organisation, and weaken the core product. Second, the organisation needs to assess whether defending the weak flanks will be sustainable in the longer term. It may be possible that these weaknesses are acceptable losses and that the contraction defence of withdrawing from the threatened markets should be used. Flanking defence should be used to defend the organisation where the loss of market share would weaken the firm, or where the market under attack is targeted for market development or product development strategies.
- *pre-emptive strike*, which is where the organisation aggressively targets the market under consideration by the competitor. In this strategy, the organisation can use market penetration (Chapter 7), market development (Chapter 8) and product differentiation (Chapter 11) in an attempt to capture a large portion of the remaining share of the market. This is a high-risk strategy in that it requires the firm to commit heavily to securing the market against a potential competitor who may enter the contested market with a superior value offering and capture the market share anyway. The pre-emptive strike pattern is designed to act as a market signal to reduce the perceived attractiveness of the market for the competitors (Chapter 5).
- *counter-offensive*, which is where the organisation attacks its competitor's market share using a frontal attack or flanking attack. The purpose of the counter-offensive is to force the competitor to commit resources to the defence of its core market share, and divert attention away from the offensive strategy. The counter-offensive differs from the pre-emptive strike in that pre-emptive strikes target the organisation's own market, whereas counter-offensives target the competitor's market. This is a high-risk strategy which combines the risk elements of the frontal or flank attack (Chapter 6) with potentially requiring investment in new market development, new product development or a diversification strategy in order to successfully attack the competitor's core market.
- *mobile defence*, which is a form of defensive strategy where the organisation defends its market share by matching or exceeding the value offering of its competitors. This form of strategy is lower-risk in that it involves a reactive alteration of the value offering based on meeting and exceeding the competitive offering, which allows for the use of the relative competitive advantage components of product differentiation (Chapter 11) as a defensive measure. In addition, mobile defence can be a non-confrontational strategy of increasing the value offering to the current market share, and can be leveraged into a fortification strategy.
- *contraction defence*, which is where the organisation withdraws from non-core markets rather than expend additional resources to compete with a stronger

opponent. This style of defence can be used to counter flanking attacks by withdrawing from weaker markets to focus resources on core business areas or to use the resources for a counter-offensive operation. In addition, contraction defences can be used as part of a divestment strategy where the organisation increases cash flow by selling off the weaker area to competitors. Alternatively, it can be the basis for cost leadership as the organisation reduces overall costs by no longer servicing the lower-margin customers in favour of focusing on the core business.

Table 13.1 outlines the summary of the types of defence, and their most common use against the types of offence approach (Chapter 6).

TABLE 13.1 Defensive tactics summary

Defensive tactic	Possible counter to . . .	Related marketing strategy
Fortification	Frontal attack Flanking Guerrilla Non-confrontational tactics	Market penetration Cost leadership Niche marketing
Flanking	Flanking	Market development Product development
Pre-emptive strike	Frontal attack Flanking Encircling Bypass	Market development Product development Cost leadership Product differentiation
Counter-offensive	Frontal attack Flanking Encircling Bypass Guerrilla	Product development Cost leadership Product differentiation
Mobile	Frontal attack Flanking Guerrilla	Market penetration Product development Cost leadership Product differentiation
Contraction	Flanking Encircling Bypass Guerrilla	Market penetration Cost leadership Niche marketing

Types of defensive marketing strategies

Defensive marketing is not a single functional approach, instead, it consists of multiple alternatives including:

- *defensive market leadership strategies*, in which the organisation moves to dominate the declining market to ensure the long-term survival of the organisation and the marketplace. This approach relies on the organisation aiming to be the profitable survivor of the decline in the marketplace through acquiring the majority share of the remaining market from its competitors (Proctor 2000; Doyle 2002).
- *defensive maintenance strategies*, in which the organisation defends its current market share, reinforces customer relationships, and uses the principles of market penetration and product development for increased customer satisfaction and loyalty, rather than increased sales or market share. Often, this is referred to as a 'middle-of-the-road' approach where the organisation attempts to either dominate a weak market or maintain a weaker presence, such as a follower position, in a stronger market. The purpose of the maintenance strategy is to develop a BCG Growth Share Matrix cash cow.
- *defensive niche strategies*, in which the organisation narrows its focus to serve the smaller, less price-sensitive niches within a mature or declining market segment. Niche strategy was covered in Chapter 12. For the purpose of defensive marketing, niches can arise as a result of 'sacking' less profitable customers and decreasing the size of the market being served by the organisation to create sustainable niches from larger market segments.
- *defensive harvest strategy*, in which the organisation plans a staged strategic withdrawal from a market whilst maximising its cash flow. This is conducted by reducing the organisational commitment to the market in the form of reduced capital investment, reduced overheads and increased prices so that the organisation can still attempt to recoup a profit margin on the product as it is being withdrawn. Harvest strategies that are successful in paring back the market can result in niche strategies or, if the product loses too many customers, may force the organisation into a divestment strategy sooner than anticipated.
- *defensive divestment strategy*, which is where the organisation exits the market after the product is deemed no longer sustainable, appropriate or desirable by the organisation. Divestment can be through selling off the function of the organisation to a competitor, or through shutting down the organisation's operation in that market.

Table 13.2 outlines the interconnection between defensive marketing strategies, defensive tactics and the offensive marketing growth strategies of Chapters 7–12).

Defensive market leadership strategy

Defensive market leadership is a paradoxical strategy which involves the organisation attempting to dominate a declining market through rapid growth, market share acquisition

TABLE 13.2 Interconnection of defensive strategies and tactics

Defensive marketing strategy	Defensive tactics	Related offensive strategy
Leadership	Fortification	Market penetration
		Cost leadership
		Niche marketing
	Pre-emptive strike	Market development
		Product development
		Cost leadership
		Product differentiation
Maintenance	Fortification	Market penetration
		Cost leadership
		Niche marketing
	Flanking	Market development
		Product development
	Mobile	Market penetration
		Product development
		Cost leadership
		Product differentiation
Niche	Flanking	Market development
		Product development
	Mobile	Market penetration
		Product development
		Cost leadership
		Product differentiation
	Contraction	Market penetration
		Cost leadership
		Niche marketing
Harvest	Contraction	Market penetration
		Cost leadership
		Niche marketing
Divestment	Contraction	Market penetration
		Cost leadership
		Niche marketing

and often competitor acquisition in order to be the profitable survivor in the market (Proctor 2000). This approach includes using cost leadership (Chapter 10) to enable the organisation to price the competitors out of the declining market. Essentially, it represents an aggressive growth strategy that is used as a form of market signalling to announce the organisation's intent to be the profitable survivor in the marketplace (Chapter 5). Engaging in defensive

market leadership involves minimising the number of competitors in the market using options such as:

- *price wars*, which depend on effective cost leadership (Chapter 10) to enable the organisation to sustain lower prices than the competitor until the competitor withdraws from the market or suffers major market share loss
- *merger and acquisition of rival organisations*, which may be included in the diversification strategy (Chapter 2) as the organisation acquires its former competitors (Doyle 2002; Proctor 2000).

Further, where the organisation is competing in a broad market, it may also require the capture of the profitable niche markets, thus placing the aggressor organisation in frontal attack or flanking attack positions with the entrenched niche suppliers. Where the market consists of a range of niches, this may also require the organisation to use product development strategies to meet the needs of the niches. Alternatively, it can seek to acquire the existing providers within the niche as part of a diversification and acquisition strategy. Finally, if the organisation is a niche provider, it needs to dominate the niche to create barriers to market entry in the form of relationship marketing and long-term contractual obligations. This is particularly important as a defensive measure where a competitor has signalled its intention to attempt market leadership of the broader market or industry in which the organisation's niche is located.

Risks of defensive market leadership

As a defensive strategy, market leadership represents a high-risk approach in that the organisation may not be able to dominate the declining market, or may end with a 'winner's curse' market. 'Winner's curse' is an economic term for when an organisation or individual invests more in the acquisition of product or market than the market is worth. Defensive market leadership is liable to the 'winner's curse' situation, particularly where the organisation misunderstands the rate of decline of the value of the market, or where the organisation becomes focused on beating a competitor rather than on the rational economics of the value of the market.

Defensive maintenance strategies

Defensive maintenance strategies occur where the organisation moves from a growth-orientated approach to customer acquisition and retention, to a fortification-style approach to defending the current market share. The organisational objectives shift from expansion to protecting the current position through three approaches as outlined by Best (2005). The approaches are:

- *to build customer retention*—the organisation focuses on strategic customer retention through relationship marketing
- *to protect market share through market barriers*—a defensive tactic based on fortification

- *cost leadership and product differentiation*—as mechanisms to match or better competitor offerings as part of a mobile defence tactic.

Defending the share: strategic customer retention

Strategic customer retention has been raised as part of the market penetration strategy (Chapter 7) and within the product development strategy framework (Chapter 9). Further, one of the core components of the 2004 definition of marketing is the management of the customer relationship for organisational and stakeholder benefit. In defensive maintenance strategies, the management of the relationship is based on maintaining current market share through customer loyalty. Although Whitwell, Lukas and Doyle's (2003) keys to retaining customers were designed for a growth strategy, they can be converted for defensive use. The five steps for defensive customer retention include:

1. *customer selection and prioritisation*, which involves determining which customer groups are the highest priority to retain, and which the organisation could lose without suffering major losses. This step can also assist other defensive strategies. For example, if the organisation needs to engage in a contraction-based defence strategy, the prioritisation process will identify the most profitable niche groups within the current customer groups. As the market matures and declines, the organisation will need to terminate relationships with less profitable customers to focus resources on the defence of the more sustainable and profitable market segments.
2. *value proposition customisation*, which is part of the cost leadership, product differentiation, and the mobile defence approach. Customer retention requires a commitment to customer satisfaction through ongoing product development, differentiation and research, and as such requires the organisation to continue to commit resources to the development and refinement of the value offering.
3. *value enhancement*, which is where the organisation increases the utility of the value offering to the customer, either through product differentiation (Chapter 11) or as part of the market penetration techniques (Chapter 7). As the size of the market diminishes, it will also increase the utility of the value offering as customers find fewer alternatives to satisfy their ongoing needs.
4. *loyalty tracking and satisfaction monitoring*, which is the core market research and information gathering process of the internal analysis (Chapter 4) during a defensive marketing strategy. Market maintenance is dependent on continued satisfaction of customer needs, which is dependent on monitoring of customer satisfaction levels.
5. *complaints follow-up and custom product development*, which is the process of investigating customer dissatisfaction with the organisation's value offering. As the size of the market decreases, the remaining customers and organisations have the opportunity to create closer business relationships and customised value offerings.

Whilst customer retention is not unique to the defensive maintenance strategy, it plays a specific role of building market entry barriers, and increasing the level of fortification over the market share.

Protect market share through market barriers

Creating market entry barriers is an important part of the defensive maintenance strategy as the organisation attempts to dissuade new competitors from entering the market. Barriers to market entry have been mentioned in passing as part of Porter's (1980) Five Forces Model (Chapter 2) and the Five Forces checklist (Chapter 5). Approaches for raising the market barriers in niche strategies (Chapter 12) include:

- *exclusivity arrangements*, which can be made with suppliers and distributors in order to encircle a market (Chapter 6)
- *relationship marketing*, which covers any attempt to lock in long-term contracts, and relationships with high-value customers (Chapter 1)
- *social expectations*, which is where membership of the niche becomes associated with a social message (Chapter 12)
- *technical, legal and patent barriers*, where the organisation blocks new competitors through non-marketing techniques such as patents on key elements of the value delivery process (Chapter 4).

Additional marketing barriers can include:

- *capital requirements to create a competitive value offering*, which is the size of the investment required by the potential newcomer to enter a market which may be on the verge of decline. Maintenance strategies can effectively raise the cost of the capital investment required through use of cost leadership strategies. In particular, cost leadership gained through internal efficiencies, capacity utilisation and production process experience will be difficult for a competitor to replicate cheaply or without significant capital investment.
- *limited untapped market share*, which is where the newcomer will have to compete directly with existing products in flanking or frontal attacks on organisations currently in the market. Defensive maintenance strategies are designed to protect the organisation against the newcomer to the market or the expansion plans of competitors, through the fortification approach, relationship marketing and customer satisfaction with the value offering.
- *restricted distribution channels*, which is where retail outlets for the distribution of a new value offering are limited either by the size of the distribution channel, or successful encircling tactics by the existing competitors. Organisations using a maintenance strategy can tie up the distribution channels through just-in-time manufacturing, custom product delivery arrangements and other relationship marketing strategies.
- *limited supplier availability*, which is where the existing suppliers of raw materials and components to the market are tied to the current product providers through relationship marketing or just-in-time manufacturing. One risk of this form of encircling strategy as a defensive mechanism is that it ties the organisation to the supplier, which reduces the ability of the organisation to respond to a flanking

attack, and leaves it vulnerable to bypass attack where the newcomer to the market does not need to rely on the existing suppliers.

Cost leadership and product differentiation

The third and final element of the defensive maintenance strategy is to protect the organisation's market share through the ongoing satisfaction of the customer's needs. Whilst this is a routine part of the organisation's business operation, it will require continued investment in research and development, product differentiation and market research, which can conflict with cost leadership strategies (Chapter 10). Organisations which plan to defer investment in maintaining and upgrading value offerings in a mature market should consider switching from maintenance to harvest strategies.

Assumptions of the defensive maintenance strategy

Defensive maintenance strategies are based on four assumptions regarding market and industry conditions:

- *market maturity*, which is where the whole strategy is underpinned by the market having reached the maturity phase of the product life cycle (Chapter 2). Whilst organisations may elect to cease pursuing growth targets at any point in the product life cycle, the defensive nature of the strategy with the emphasis on fortification assumes the market conditions match those of maturity or early decline.
- *sustainable revenue*, which underpins the financial rationale for engaging in maintenance strategies. Where the organisation is no longer facing a sustainable revenue from a market, it needs to engage in harvest or divestment strategies.
- *market and industry stability*, which is the assumption that growth and decline levels will be relatively static, and that the market will not suddenly collapse. The assumption of stability also assumes the number of competitors and their relative market share holdings will remain reasonably constant.
- *barriers to market entry*, which is a companion to the assumption of market stability, as the barriers for entry are assumed to be sufficiently high to discourage competition.

Defensive niche strategies

Defensive niche strategy leverages off the exit niche strategy where the organisation is facing a declining existing niche (Chapter 12). It can also occur as a result of a defensive market contraction tactic where the organisation withdraws from expendable markets to focus its operations until they reach a sustainable niche. Defensive niches are interim measures that can result in three possible outcomes:

- *niche maintenance*, which is where the niche is reduced sufficiently to a core of non-price-sensitive customers who will continue needing the value offering, and who will continue making the provision of this product sustainable if not profitable.

- *subsidised defensive niche*, which is where the niche is no longer financially self-sufficient, but holds a tactical or strategic value as part of a market leadership fortification strategy.
- *exit to harvest or divestment strategies*, which is where the niche is maintained for as long as is necessary to either harvest the niche or secure the divestment of the product for a cash return or cessation of the value offering.

Assumptions of the defensive niche strategy

Despite being an interim strategy between maintenance and harvest, defensive niche is still underpinned by a series of assumptions, which include:

- *ongoing demand*—the assumption that there is still a core group of customers who desire the value offering.
- *non-price-sensitive customers*—the assumption that the customers still in the declining market are less price-sensitive. This creates an opportunity to increase the price of the value offerings as the surviving customers are more focused on the benefits than the costs of the value offering.
- *optimisation is possible for maintenance* or *divestment for cash is possible following the niche reduction*—in the first, the organisation assumes that it can maintain profit margins as it decreases the volume of the value offerings produced, while in the second, it assumes that after contracting the market to the core non-price-sensitive customers, the market is sufficiently attactive to a competitor or other organisation that it will purchase the organisation's operations in this area.

Defensive harvest strategy

Defensive harvesting involves cutting investment to the product in an effort to increase the cash flow and margin on the value offering (Doyle 2002; Hooley, Saunders & Piercy 2004). In effect, harvesting makes use of cost leadership methods, but without a view to the long-term survival of the product offering. This type of strategy represents the second-last phase of existence for the organisation's value offering. Either the harvesting generates sufficient cash flow to warrant revitalising and ongoing maintenance strategies, or the value offering is divested.

Harvesting is a form of a staged withdrawal that relies on maintaining a reduced position in the market all the time the market remains profitable but with the ultimate aim of divesting the value offering. This ties into the BCG Matrix recommendations for 'dog' products, along with the Directional Policy Matrix categories of phased withdrawal 1 and 2. It also runs contrary to part of the market penetration strategy of customer maintenance as it is less concerned with maintaining customer volume than with per-unit revenue. Cutting relationship marketing costs, sacking clients and removing higher-cost customers as part of the streamlining of the cash flows is part of the management of customer relationships for organisational and stakeholder benefit.

Assumptions of the defensive harvest strategy

The harvest strategy is based on a series of assumptions regarding the market, the expected maturity-decline rate, and the internal transfer of resources within the organisation. These core assumptions are:

- *the market has entered late maturity or decline*, therefore the organisation will probably lose sales as a natural part of the market decline.
- *the value offering is not a core part of the organisation*, so the organisation will not suffer losses to other product lines, positioning strategy, brands or relative conceptual advantage by harvesting or divesting the value offering. For example, as stated previously, the Harley-Davidson's 'hog' motorcycle range is core to the image of the organisation. Harvesting and divesting this iconic symbol would damage the whole of the organisation's value offerings and position in the market.
- *the decline rate in the market is stable*. The market is on a predictable decline rate so the organisation can select when to divest the harvest product.
- *harvesting is sustainable during the exit phase*, which is linked to the assumed decline rate, and also assumes that cost-cutting to increase cash flow will not deteriorate the value offering to the point where it accelerates the sales decline.
- *the cost structure is stable*, and the organisation's costs will not increase due to the reduced investment in production causing increased per-unit costs. For example, if the organisation had created cost savings based on volume pricing, or economies of scale based on certain production volumes, reducing the organisation's offering to the market below these levels may increase the per-unit costs dramatically. This will impact on the sustainability of the harvest strategy. Where this is predicted to occur, the organisation should consider maintenance to continue the per-unit cost advantage, or move straight into a divestment strategy.
- *unbalancing the portfolio will benefit the organisation*, that is, the resources currently being used in maintaining the value offering to be harvested could be put to better use somewhere else in the firm. Portfolio balancing was reviewed in Chapter 4 as a mechanism for cash flow assessment. Harvesting is a deliberate method of bringing the cash flow forward, but carries the high risk of the organisation suffering losses in the future if the cash-generating products decline before replacements are developed.

Approaches to harvesting

Determining the speed of the harvesting strategy will also influence the risks and rewards associated with the process. The two approaches (fast harvest and slow harvest) have markedly different outcomes.

Fast harvesting works on the assumption of rapid decline in existing sales where the organisation abandons investment in the value offering, and tries to recoup its investment before the product line suffers significant loss. This approach is akin to a 'fire sale' strategy, where the organisation tries to gather revenue quickly with little concern for the ongoing viability of the brand, and is usually a precursor to divesting the product portfolio.

Slow harvesting is an approach that involves a progressive reduction in the investment on the product offering, and can be coupled with the cost leadership strategy (Chapter 10). This approach aims to maximise the margin per unit without expending additional capital or resources beyond the operational and maintenance level. It can be used as a precursor to maintenance or defensive niche strategies as the organisation scales back its commitments to the market. As a slow-moving strategy, it has the advantage of being able to be reversed if the market shifts back to growth, or the organisation revitalises the demand for the product. The risk inherent with the reduction of investment is being caught off-guard by changes in market conditions, new technology or new competitor value offerings, all of which could lead to sharp decline in the relative competitive advantage of the organisation's offering. Slow harvests can also be used to prepare a value offering for sale to a competitor by streamlining the organisation's production process to maximise its appeal to potential purchasers.

Defensive divestment strategy

The defensive divestment strategy involves the organisation ceasing to offer its product to the market, and either disposing of it through sale, or simply stopping production of the value offering. Consequently, the divestment strategy is particularly suited to dealing with poor-performing strategies within the Directional Policy Matrix (Chapter 2). The preconditions for the two strategies are:

- *sell-off divestment*, where the organisation can find a buyer for the production processes of the value offering. This is most common for products with a Directional Policy Matrix rating of low strength/medium market attractiveness or medium strength/low market attractiveness.
- *shut-down strategies*, where the organisation develops an exit strategy to leave the market by terminating existing customer relationships or transferring them to competitors. This is best suited to the usually unsaleable options with low strength/low market attractiveness.

Assumptions of the defensive divestment strategy

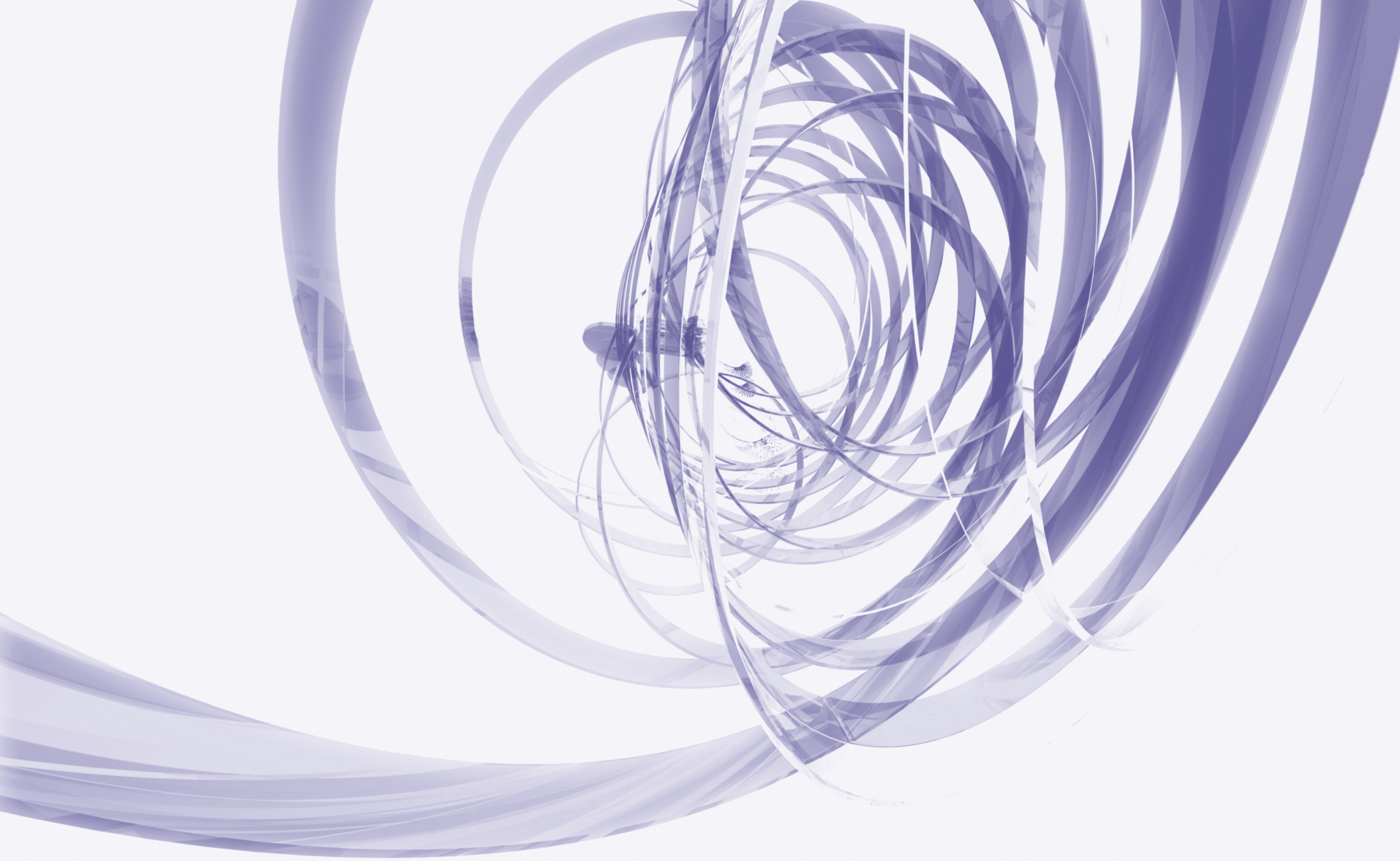
Divestment strategies are based on the following assumptions:

- *the market is in decline*, which corresponds with the low market attractiveness elements of the Directional Policy Matrix.
- *the organisation has a weak business position within the market* (which is connected to the low strength aspect of the Direction Policy Matrix), or the organisation has limited to no competitive or cost advantages.
- *there are significant price pressures*, which is where the organisation lacks a relative cost advantage, or the market is highly competitive on pricing.
- *the value offering is superfluous to the organisation*, which is where the product offering can be divested without impacting on the rest of the organisation's activities.

- *the value offering is superfluous to the market*, which is where the demand for the organisation's product has ceased, or has been replaced with a demand for alternative value solutions.
- *existing relationships can be transferred to competitors*, which is where the organisation can exit the market without penalty from contractual barriers with suppliers, distributors and customers by transferring these commitments by sale to another organisation.

Conclusion

Defensive marketing encompasses five areas of marketing strategy and business activity. The five alternatives range from aggressive offensive strategies to capture and secure a dominant position in a market, through to the defensive contraction of the organisation to a core group of die-hard customers. It can involve maintaining market share ahead of the pursuit of growth options, or as a response to declining market attractiveness. Defensive tactics can also involve harvesting value offerings for maximum cash flow or unsuccessful products can be sold off or discarded to free the organisation's resources for more viable alternatives.

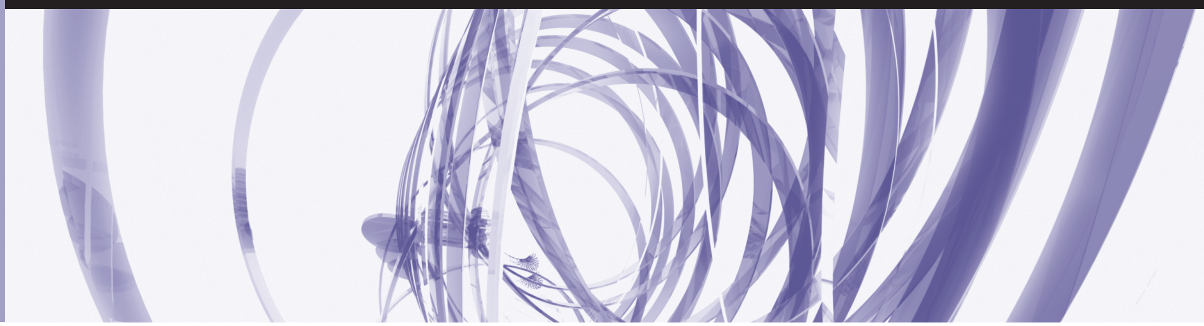


PART 4

Marketing implications

From analysis to action—The marketing plan

CHAPTER 14



Introduction

Marketing plans are essential as an ongoing influence at the corporate level to position the company in the overall business environment and at the product and market level to provide clear guidance as to the appropriate marketing mix. The marketing plan draws its broad direction from the firm's overall corporate objectives and summarises the decisions and outcomes arising from the various analyses of the market, competition and stakeholders by summarising decisions into clear action points. This chapter overviews the role and content of a strategic marketing plan. Strategic marketing plans are the final outcome of the analysis and planning phases. They provide the blueprint, or roadmap, as to what to do to achieve the organisation's strategic marketing goals. The strategic marketing plan helps to focus objectives and organisational activities into maximising the return on investment from presenting a value offering to the customers.

The marketing plan v. marketing planning

The marketing plan is the tangible output of the organisational objectives (Chapter 6), marketing planning and analysis process (Chapters 4 and 5). It crystallises and summarises the detailed discussions and decisions made during strategic marketing planning. While

there is some basis of truth in the common saying, 'plans are nothing, planning is everything', in practical terms, it is impossible for an organisation to operate strategically for long-term survival and growth based on a series of shared unwritten understandings.

Decisions made as a result of the formal process of analysis and debate need to be formally contained in a plan with clear milestones and targets. Without a plan, employees and management can easily lose their way, forget critical agreed actions and remain unaccountable for product and marketing failures.

Barriers to marketing planning

The concept of developing and implementing quality marketing planning processes and marketing plans is intuitively appealing. The benefits of having a clear and structured plan to achieve business goals have been consistently demonstrated over time. Yet despite this, there remain barriers to effective marketing planning. Common barriers to planning include:

- *a lack of understanding regarding the marketing function*, where the management or board of directors do not fully understand or adopt the marketing concept, marketing tactics and marketing strategy. This involves the product context stakeholders (employees, management, board of directors and shareholders—Chapter 3), along with the marketing element of the secondary value chain (Chapter 4).
- *lack of in-depth analysis*, where the internal (Chapter 4) and external (Chapter 5) analyses are not taken seriously by the organisation, or where key decision makers in the organisation claim to 'understand the needs of the customer' without reference to market research or the customer.
- *lack of systematic planning approaches*, where there is no managerial emphasis on medium- to long-term planning, or the organisational objectives are focused on short-term metrics (Chapter 15). This can lead to a business environment where the time invested in systematic planning can be seen as time wasted or time lost from making sales quotas.
- *organisational barriers such as organisational culture*, which is where the marketing function is poorly perceived within the organisation, where there is a corporate history of ad-hoc activities that have been moderately successful, or where success has been achieved through good fortune rather than any application of skill.
- *a lack of the key skills and knowledge necessary to develop and implement quality strategic marketing plans*, where the organisation needs to increase its investment in skilled employees. This ties into the marketing, sales effort and human resource components of the value chain (Chapter 4), along with the employee and management stakeholder groups (Chapter 3).

McDonald (2002) has developed what is referred to as the 'Ten S' approach to overcome these internal barriers to marketing planning and the development of effective marketing plans. In summary, the Ten S model consists of the following principles:

- Principle 1: Strategy before tactics
- Principle 2: Situate marketing within operations
- Principle 3: Shared values about marketing
- Principle 4: Structure around markets
- Principle 5: Scan the environment thoroughly
- Principle 6: Summarise information in SWOT analyses
- Principle 7: Skills and knowledge
- Principle 8: Systematise the process
- Principle 9: Sequence objectives
- Principle 10: Style and culture.

Principle 1: strategy before tactics

The first principle of the model is that organisational agreement on the overall marketing strategy is needed first, and then the development of the strategic marketing plan for the next three to five years should occur before any focus on managerial or tactical elements takes place. Objectives should be set to provide a framework for the strategic marketing plan (Chapter 6). The objectives and plan need to be based on a systematic analysis of the competition (Chapter 5) without which, any tactical plans will be uncoordinated and lack focus.

Principle 2: situate marketing within operations

Marketing needs to be close to the customer, not a separate and isolated department. For marketing to be effective, it needs to be integrated with other functions of the organisation, not to operate in isolation. This is illustrated in marketing's presence in the secondary value chain (Chapter 4) as part of the supporting mechanisms that create value for the organisation, and through the presence of the sales effort as a component of the primary value chain (Chapter 4).

Principle 3: shared values about marketing

All levels of the organisation need to understand the basic element of marketing in terms of what it can do for the organisation, what limits apply, and what marketing contributes to the organisation. Without this shared understanding, the marketing planning process and the implementation of marketing plans will be impeded. Unless the whole of the organisation shares a commitment to the marketing orientation, marketing will not reach its potential in meeting market needs and serving the target market.

Principle 4: structure around markets

Wherever possible, organisational functions should be developed around serving specific markets instead of functional lines, as demonstrated repeatedly through the integration of the marketing component into the value chain. An integrated program of marketing, finance, strategy and manufacturing designed to serve the organisation's target market is more likely to result in quality outcomes for the overall marketing strategy of the organisation. In contrast, separating marketing from finance will possibly create friction where marketing attempts a cost leadership strategy without the support of the finance section. Alternatively, if price setting is external to the marketing department, the finance section

may set a price that does not support the product's position, IMC or branding. Effectively, the organisation needs to develop specific value chains that focus on markets, rather than dividing the organisation along functional lines of finance, strategy, marketing or production.

Principle 5: scan the environment thoroughly

Effective marketing strategy and planning relies on access to timely, accurate and useful information. Whilst all marketing strategy is necessarily built on less than perfect information due to the nature of market research, market analysis and availability of key information, effective marketing scanning can be performed through a marketing audit. McDonald (2002) presents a five-part marketing audit model which includes the following components:

- *explicit statements of the issues facing the organisation*. The marketing audit is aimed at addressing specific issues facing the various business units internally and externally.
- *checklists and questions*, which form the basis of the firm's marketing information system to ensure the requisite information required for the planning process is collected.
- *customised questions*, which are designed to specifically address the information needs and concerns of each level of the organisation involved in the marketing planning process.
- *formal analyses based on the structured analytical models*, where the organisation structures its marketing information collection around the use of various key strategic models (Chapter 2) internal analysis frameworks (Chapter 4), external analysis techniques (Chapter 5), and any strategy-specific model (Chapters 7–13).
- *mandatory and ongoing activity*. The organisation is required to continually update the marketing audit. Converting the perception of the marketing audit activity from a single snapshot of the market to an ongoing part of organisational activity will improve the quality of the marketing information collected. In addition, defensive marketing strategies, such as harvest, which depends on knowing when to maximise cash flow and when to shift to a divestment strategy, are dependent on monitoring changing market conditions to be effective. Ongoing marketing audits will also assist product differentiation (Chapter 11) and market penetration (Chapter 7).

Principle 6: summarise information in SWOT analyses

Information gathered as a result of the marketing audits in Principle 5 should be summarised in a SWOT analysis to provide the intelligence needed to develop the marketing strategy and plan. The SWOT analysis is a method of reporting marketing information that summarises the organisation's position in terms of:

- *strengths*, which is equivalent to the business strength component of the Directional Policy Matrix. This draws primarily on the internal analysis (Chapter 4) but can also include factors such as relative competitive advantage (Chapter 11),

relative cost advantage (Chapter 10) and assessments of customer retention and loyalty (Chapter 7).

- *weaknesses*, which is the most important factor in any analysis, and lists any relative competitive disadvantage, relative cost disadvantage or any other information regarding organisational underperformance or failings. This ties into the low competitive position aspect of the Directional Policy Matrix. Further, it also assists in developing defensive tactics where the organisation can identify weaknesses such as underdeveloped flanking markets, or poor-performing areas that can be divested in a contraction defence.
- *opportunities*, which equates to the GE Matrix industry attractiveness, and the market attractiveness element of the Shell Chemical Directional Policy Matrix. Opportunities represent the combination of external analysis (Chapter 5), objectives (Chapter 6), potential growth strategies (Chapters 7–9) and value addition (Chapters 10–12).
- *threats*, which are those factors that pose a danger to the organisation, a challenge to the market share or could cause potential problems for the organisation. This includes shifts in the product life cycle (Chapter 2), changes in the industry uncovered by industry analysis (Chapter 5), arrival of new competitors (Chapter 5), or problems that arise from the risks associated with the implementation of the different strategy areas (Chapters 7–13).

Principle 7: skills and knowledge

The seventh principle involves ensuring that those responsible for developing marketing strategies and marketing plans have the necessary skills and knowledge to make sense of the collected intelligence and apply it in ways designed to 'sell' the strategy internally and maximise organisational outcomes. This ties into the employee and management stakeholders (Chapter 3), along with the human resources, marketing and sales effort aspects of the value chain, and the internal analysis of the organisational resources (Chapter 4). As mentioned earlier in the chapter, a lack of key skills and knowledge is one of the major barriers to the implementation of marketing plans and planning processes.

Principle 8: systematise the process

The larger the organisation the more important it is to document the processes of planning to ensure that a common approach to developing marketing plans is implemented throughout the organisation. This consistency makes it easier to ensure that all business units have engaged in the depth and level of planning appropriate to their responsibilities. Principle 8 connects to the systems and marketing components of the value chain (Chapter 4).

Principle 9: sequence objectives

The planning process will generate a range of objectives that need to be prioritised. Criteria for prioritisation of objectives includes their impact on the organisation and their urgency so that limited resources, both human and financial, can be allocated accordingly. Chapter 6 focused on the different criteria for objective-setting and prioritisation techniques which have been used in range of areas throughout the book.

Principle 10: style and culture

The final step of the Ten S approach is to ensure the marketing plan fits the style of the organisation, the organisational culture, and the life cycle phase of the organisation. Organisational culture can support or undermine the whole process from planning through to implementation. Consequently, the stakeholder needs of the employees and management need to be incorporated into any marketing plan to increase the likelihood of support within the organisation. Simply having a plan or a planning process in place does not guarantee support. Without taking steps to build support for the concept of marketing, the marketing process and the marketing plan, the activities simply become a routine with no tangible outcome or contribution to the firm. The process of gaining intra-organisational support for the marketing plan and strategies is covered in more depth in Chapter 15.

Value of the marketing plan

Marketing planning is necessary for sustainable success for a variety of business reasons. In summary, the reasons include:

- *increased complexity of the business environments*, including the increased expectations of the external stakeholders and the increased role of the stakeholder under the 2004 definition of marketing.
- *improved technology*, which increases the availability of marketing information systems and increases the volume of data which needs to be translated into workable marketing information.
- *increased competition*, which is arising from national and international markets, globalisation, widespread access to the internet and accelerated product life cycle curves due to technological advances.
- *altered regulation conditions*, including the increase in the levels of shareholder expectation of managerial and director accountability for failure, and the shift in government stakeholder expectations towards industry deregulation.
- *greater access to international markets*, which has increased opportunities for business, and at the same time led to increased competition in areas previously regarded as national or local markets.

For a business to succeed, it needs to be aware of sources of competition and of changes in the market which lead to greater opportunities, and have a concise set of actions in place to achieve its goals. The benefits of creating a marketing plan include that it summarises these trends, opportunities and actions in a succinct document. The marketing plan assists the organisation in the following areas:

- *identifying opportunities*, which is where the process of analysis that underpins marketing planning helps the business to uncover opportunities that may not be immediately obvious to the employees or managers in daily operations.
- *leveraging core capabilities*. A well-designed marketing plan can make better use of existing business competencies, business systems and unique characteristics of

the organisation across a range of products and markets. This interconnects with the cost leadership strategies (Chapter 10), product differentiation (Chapter 11) and niche strategies (Chapter 12).

- *focused marketing strategy*, which is the ability of a specific marketing plan to unify the different areas of strategic and tactical marketing functions with a specific focus, coherent strategy and set of tactics to implement a marketing campaign to support the organisation's value offering or market position.
- *resource allocation*, which is where the plan can be used to clearly define what target markets will be engaged by the organisation. A focused marketing plan provides a framework for the effective allocation of financial and non-financial resources for the organisation.

Types of marketing plan

Within any given organisation, there will be a number of different marketing plans. The larger the organisation is, the more likely it is to have a variety of marketing plans in place at different levels, for different lengths and for different purposes. For example, in a university context it is usual to have an overall corporate marketing plan, which supports the overall positioning of the university (such as quality research, small classes, or teaching excellence). Multi campus universities also tend to have campus-specific marketing plans along with individual faculty plans. Even within faculties, schools or departments will develop their own plans, which are often further divided into specific market plans such as the marketing plan for undergraduate students, post-graduate students, international students, research higher degree students and so on. The danger that large organisations face, is the potential for inconsistency among this wide variety of plans and strategies directed at different markets.

To minimise such problems, all marketing plans should derive their strategic direction from the overall corporate strategic plan. If all plans are aligned with the core positioning strategy of the organisation, a reasonably high degree of consistency is possible while maintaining the flexibility to engage segment-specific strategies to maximise market penetration.

Marketing plans can be created at the following levels and for the following purposes:

- *corporate level*, where the marketing plan positions the whole of the organisation within the overall market or industry. These plans are responsible for communicating the core values of the organisation to the broader public and stakeholders.
- *market segment*, where plans position a range of the organisation's products within a target market. Market segment-focused plans are strongly image-orientated, and can be used to create relative conceptual advantages (Chapter 11), personality niches (Chapter 12) and branding (Chapter 2).
- *value offering or product level*, where plans focus on a specific value offering. Product level plans are highly targeted, and derive their image and positioning from the broader corporate or segment plans but are more focused on

communicating specific information and value to the market. These can be used for communicating product differentiation (Chapter 11), or supporting growth strategies (Chapters 7–9).

In addition to the different levels at which the marketing plan can be focused, there are two key types of plan:

- *strategic marketing plans*, which are those marketing plans of medium-term (approximately 3 years) duration that set the overall direction of the marketing strategy.
- *tactical marketing plans*, which are those shorter-term (usually 1 year) marketing plans that derive their direction and objectives from the strategic marketing plan and are highly focused on specific markets or products. Tactical marketing plans implement the different elements of the overall marketing strategy. In addition, given that these types of plans are modified on at least an annual basis, they provide the mechanism to allow for flexibility in the implementation of the strategic marketing plan.

To further complicate the issue, many organisations further sub-divide their tactical and strategic marketing plans along component function lines. This creates the additional category of plans:

- *product mix plans*, which outline intended product deletions, modifications and additions as well as predicting volume, turnover and profit.
- *sales plans*, which specify the service levels anticipated for existing accounts (relationship building and re-sales) as well as setting goals for gaining new sales or accounts.
- *advertising plans*, which focus specifically on the timing, nature and amount of advertising as well as advertising objectives (e.g. awareness raising, sales, brand image), media and overall budgets for these activities.
- *sales promotion plans*, which are for specific activities such as competitions or price reductions aimed at stimulating short-term demand (Proctor 2000).

Table 14.1 outlines the different types of plans and their interconnections with different areas of marketing strategy theory and practice.

The larger and more complex the organisation and its product lines are, the greater the number of different marketing plans that will be developed. The key to organisational effectiveness is to ensure consistency and coordination between plans, which is best achieved by quality communication within the organisation and strict adherence to the ideals and aims articulated in the corporate level strategy. Regardless of the level or focus of the marketing plan, a degree of flexibility is essential to allow the tactics created to implement the strategy to be adjusted regularly to adapt to changing market conditions. Further, it is important to regularly update and revise forecasts and goals in the light of organisational success or failure and to adapt to any changes in the market.

TABLE 14.1 **Interactions between plans and marketing strategy theory**

Type of plan	Summary	Connections
Corporate level	Positions the whole of the organisation within the overall market Is responsible for communicating with public and stakeholders	Stakeholders (Chapter 3) Objectives (Chapter 6)
Market segment	Positions a range of the organisation's products within a target market	Relative conceptual advantage (Chapter 11) Personality niches (Chapter 12) Branding (Chapter 2)
Product level	Is a plan for a specific value offering	Product differentiation (Chapter 11) Growth strategies (Chapters 7–9)
Strategic marketing	Medium-term plan Sets direction of the marketing strategy	Marketing strategies (Chapters 7–13)
Tactical marketing	Shorter-term marketing plan focused on specific markets or products	Niche marketing (Chapter 12) Product differentiation (Chapter 11) Product development (Chapter 9) Market development (Chapter 8) Market penetration (Chapter 7)
Product mix	Intended product deletions, modifications or additions Predicts volume, turnover and profit	Product development (Chapter 9) Product differentiation (Chapter 11) Harvest and divest strategies (Chapter 13)

Sales	Specifies the service levels anticipated for existing accounts Sets goals for gaining new sales or accounts	Sales effort (value chain) (Chapter 4) Product differentiation (Chapter 11)
Advertising	Timing, nature and amount of advertising Advertising objectives Media purchase Budgets	Relative conceptual advantage (Chapter 11)
Sales promotion	Competitions Price reductions	Market penetration (Chapter 7) Cost leadership (Chapter 10) Growth strategy (Chapters 7–9)

Creativity v. structure

Another of the ongoing debates in marketing is whether marketing is a science or an art. This tends to come into debate in the final stages of the strategic marketing process, when the question is raised: 'to what extent is the marketing plan a pro forma structured template that can be applied across all marketing situations?'

Effective marketing strategy requires a high level of objectivity and skilled analysis. At varying points of the analytical process different models are applied to make sense of the complex marketing and organisational environment (Chapters 4 and 5). Further, at other stages of the external analysis, experts in finance, logistics, manufacturing and other functions integral to a successful marketing strategy have technical input into the analysis, planning and decision-making processes.

The strong reliance of strategic marketing on hard facts on which to base decision making does not preclude a level of creativity. Similar organisations face the same objective external realities (market opportunities, market size, potential segments, spending power of the segments and stated consumer preferences) and each will develop a unique marketing strategy and position to meet these challenges. At any given time an organisation will be faced with a range of equally attractive, yet incompatible, strategic options. It is at this point that marketing personnel must exhibit a degree of flexibility and creativity.

Creativity in marketing is not confined to the tactical elements of promotional design. It is integral to the decision-making process which takes a variety of independent analyses and makes sense of them to form an integrated whole. In the same way, while the structure of a strategic marketing plan may be similar across organisations, and there are certain elements that must always be included, the content and approach varies considerably

between organisations in the same industry. Losing sight of the need to infuse a creative element, albeit based in the outcomes of rational analyses, reduces the marketing plan to a pro forma of little strategic value. Using the analogy of art, Best (2005) summarises this dilemma as follows:

> The creative use of light and colour can make a picture interesting and appealing, but without some degree of form to add meaning to the composition, the picture may be intriguing but confusing. On the other hand, all form and no creative expression yields a sterile picture. The same is true for a marketing plan: both creative insight and analytical structure are necessary to paint a meaningful picture of the market situation, marketing strategy, and logic based path that connects desired performance objectives with marketing strategies. (p. 406)

The key function of the marketing plan is to provide that logic-based pathway in a defined and accessible form so that all members of the organisation share a common understanding of where they are going and how they will get there.

Format of the marketing plan

There are many different books, software programs and templates available for developing the final 'marketing plan' document. Each format will differ slightly according to the preferences of the marketer, organisation or writer, however all are equally valid as long as they answer the following questions:

- Where are we now? (situation analysis, Chapters 4 and 5)
- Where do we want to go? (objectives, target market selection, positioning strategy, Chapter 6)
- How do we get there? (marketing mix, resources, implementation plan, Chapter 14)
- Where did we end up? (controls and marketing metrics Chapter 15)

Ultimately the purpose of the marketing plan is to capture, in writing, the outcomes of the analyses and processes of planning that precede it. The plan represents the conclusions and outcomes of the process at a specific point in time. A good marketing plan will provide clear guidelines, while allowing for regular review and flexibility to adjust to the ever-changing marketplace. Once a plan starts to be implemented, the environmental and competitive situation will inevitably change as customers respond to the campaign, either positively or negatively, and competitor organisations take appropriate reactive action.

For the purposes of this text the following headings derived from Proctor (2000) are used as the framework for the marketing plan:

- overview
- background or situation analysis
- objectives
- positioning (including target market selection)

- strategies and tactics focusing on the marketing mix
- budget
- evaluation plan.

Overview

The overview to the plan consists of three parts:

- executive summary
- table of contents
- introduction.

Executive summary

The executive summary is the synopsis of the entire plan, and summarises the key elements of the plan, including:

- the strategic direction of the plan
- the competitive advantage of the product
- the investment needed to achieve the objectives of the plan
- the anticipated outcomes.

The executive summary, as the name implies, is a *summary* of the entire plan and, as such, needs to address the critical points raised in all elements of the plan. For many executives, managers and investors, the executive summary determines whether or not they will read the whole plan. It should be succinct yet comprehensive, well written and easy to read. Although it is the first element of the plan to be read, the executive summary should be the last part of the plan to written.

Table of contents

Like the executive summary, the table of contents provides readers with a quick and easy overview of the plan. Most marketing plans are assessed by a board or committee consisting of members from a variety of functional areas. The key benefit of including a table of contents, irrespective of how short the overall plan is, is the ease with which readers can find the information they need to make a decision. For example, financial analysts will have limited interest in the communications strategy but rather will focus on the predicted costs, return on investment and break-even analysis.

Introduction

The introduction to the plan provides an overview of the background to the plan. Unlike the executive summary, the introduction does not provide a synopsis of the whole plan but rather a statement of the background to the marketing strategy, and includes:

- an overview and description of the product
- the motivation behind the marketing strategy
- the company's mission statement or statement of corporate intent.

Background or situation analysis

The situation analysis provides the specific context to the marketing strategy. It summarises the outcomes of the internal (Chapter 4) and external (Chapter 5) analyses and their impact on the development and implementation of the marketing plan. Cohen (2001) divides the situation analysis into four distinct areas:

- *situation environs*, which include demand and demand trends for the product, social and demographic trends, economic and business trends for the product, state of technology and the stage in the product life cycle, political trends which may impact on the product, and marketing strategy and legal issues. This involves Porter's (1985) industry analysis and the environmental context stakeholders (Chapter 3).
- *neutral environs*, which are the groups or organisations likely to impact on the company and its marketing strategy, including production context stakeholders such as distributors (Chapter 3).
- *competitor environs*, which are those firms which are competing with the organisation and its product (Chapter 5). Included in this analysis should be an outline of who these competitors are, the products they offer, their organisational strengths and weaknesses, distribution channels and likely future activities. As with the situation environs, this aspect involves part of Porter's (1985) industry analysis along with the competitor stakeholders (Chapter 3).
- *company environs*, which describes the situation of the company and the resources it has available as determined by the internal analyses (Chapter 4). Included in this section is an overview of current products, experience, expertise, financial, human and capital resources, suppliers and relationship with current customers. This involves the production context stakeholders of employees, management and suppliers, along with a review of the customer as stakeholder. The 'company environs' area also interconnects with value chain analysis (Chapter 4).

Market segmentation, target market and positioning

Having outlined the current state of the organisation and the broader competitive conditions, the next step is to narrow the focus. Few products are universally attractive; hence the need to segment the market and focus on one or more key target markets. Segmentation and target market selection form part of the core of growth strategies (Chapters 7–9), product differentiation (Chapter 11) and niche strategies (Chapter 12). Details of segmentation appear in Chapters 2 and 6.

Market segmentation

In this section the bases of market segmentation used in the marketing strategy are outlined, along with the size of the overall market. This section is used to report how the prioritisation of the most attractive market segments is estimated and the bases used in

the segmentation strategy are justified. Having thoroughly analysed the potential market and potential market segments, an appropriate segmentation strategy (niche, concentrated or multiple segmentation strategy) is chosen and the reasons for making this choice ahead of the alternatives outlined.

Target market

Based on the criteria for a 'good' marketing segment—that is that the segment is measurable, accessible, responsive and substantial (Chapters 5 and 6)—a decision is made as to which market or markets the company will address. If a multiple segmentation strategy is chosen, and the needs of those different segments are sufficiently different, it may be necessary at this point to create alternative detailed marketing plans for each of the target segments. Again the focus here is not only on the choice of target market(s) but the reasoning behind that choice.

Positioning

Positioning refers to the relative place the organisation and its products occupy in the mind of the consumer (Chapters 2 and 11). The marketing plan can only review the current position and highlight the preferred or intended position for the organisation. The choice of variables or characteristics on which to base the positioning strategy needs to be identified and justified. A statement of the intended position of the product needs to be given along with an overview of where the product sits relative to its competition.

Marketing goals and objectives

At this point, and in light of the issues raised in the preceding analyses, the specific goals of the marketing strategy can be stated. Chapter 6 discusses in detail how marketing objectives are derived. In this section the focus is on clearly stating what the organisation hopes to achieve by implementing the marketing plan. Depending on the type of marketing plan under consideration, the objectives can be timetabled to be achieved in a period of (for example) from one to five years. For example, the five-year strategic objective may be to have the second-largest market share in the industry. To achieve this, the first specific annual objective may be to increase current market share by 20 per cent.

Marketing objectives must be derived from the analyses previously conducted and be specific and measurable. Further they must be consistent with the overall direction of the organisation, its total positioning strategy, branding and image, and be realistic within the confines of the marketplace, competitors and resources available. The marketing objectives set the framework for the development of the specific blend of marketing mix tactics designed to achieve these goals.

Strategies and tactics focusing on the marketing mix

This is the section that develops the specific strategies and actions designed to achieve the goals and objectives set. The marketing mix strategies and tactics must be consistent with the organisation and its goals. Further they must also blend well together and be

designed to work as an integrated whole to support the overall strategic position in the marketplace.

Different strategies are appropriate for each element of the marketing mix, depending on what the firm's objectives are, what its capabilities are and, more generally, at what stage in the life cycle the product is positioned. Depending on the magnitude of the project, and what the overall strategic marketing plan is trying to achieve, sub-plans can be developed for each element of the marketing mix. This is most likely to happen with the promotional element, where separate sales and advertising plans will form a subset of the total marketing plan. The following section will consider the tactical options available to marketers for each element of the marketing mix in turn.

Product

The extent to which 'product' strategies feature more or less prominently will depend on the overall strategic direction of the marketing plan. Inevitably if the organisation is pursuing a new product development strategy (Chapter 9), product will feature more prominently than if the firm is keeping the same products and pursuing a market penetration (Chapter 7) or market development strategy (Chapter 8).

Product will help drive the development of the other marketing mix strategies. In particular, experience has shown that at different stages of the product life cycle, the sub-objectives within each element of the marketing mix, and the tactics used to achieve these, will vary in a predictable pattern as outlined in Table 14.2.

TABLE 14.2 Marketing mix tactics across the product life cycle

Marketing Mix	Introduction	Growth	Maturity	Decline
Product	Basic model	Minor variants	Wide range of options	Basic model
Price	Penetration Skimming Market-based	Market-driven Penetration pricing	High price-competition Prestige	Low price-competition Relatively high price
Place	Minimal outlets	Increased availability	Intensive distribution	Minimal outlets
Promotion	Build awareness	Brand development	Highly differentiated	Information-based

While the table outlines the typical strategies employed at the different stages of the product life cycle, within each stage variations occur depending on organisational objectives and positioning strategy. For example, if a product is positioned as a high status,

high quality prestige product then it will maintain a relatively high price and exclusive distribution throughout the product life cycle irrespective of the general trends for the product category.

Price

From the organisation's point of view there are three basic pricing strategies within which a range of tactics can be developed. These are to price the product:

- *above the market*, at a price premium that has to be supported through a relative competitive advantage
- *at the market*, where the organisation is on price parity with its competitors
- *below the market*, which needs to be supported by cross-funding from other parts of the organisation, or rely on a relative cost advantage (Chapter 10).

Again the decision to choose one level of pricing ahead of the others is based on positioning decisions. Final price is based on:

- *cost considerations*. The basis of price setting is organisation-focused and involves determining how much per unit the product costs to produce at different output levels, and then adding a discrete amount to the cost price to ensure a given level of profit per item. This margin can be based on a percentage of overall cost or a fixed dollar amount.
- *value perception pricing*, which is consumer-focused and relies on quality market research to determine how much the market is prepared to pay for different product and then set the price based on the findings of the research. This relies on the organisation's relative competitive advantage being valued by the market. Once the price has been set by the market, the organisation will work backwards to determine whether or not it can produce the product profitably at that price level.

A form of value-based pricing that is common for large purchases and in the business-to-business sector is economic value to the customer (EVC). Using EVC the customer determines the total lifetime cost of the product by considering not only the acquisition cost of the core product but also how much it costs to run, likely repair costs, resale value and so on. Understanding consumer perceptions of the lifetime cost of a major purchase allows flexibility in pricing the core product. In some cases, such as printers, the core product may be priced close to cost or even below in the knowledge that the lifetime value of the customer purchasing ancillary products to use the product will make up this shortfall in the long term.

Due to common psychological price/quality associations, those organisations that choose to price above the market must support this tactic by providing a product of superior perceived value. While prestige pricing is a sustainable above-market pricing tactic, price skimming is also common when introducing new product variations to the market. The difference between prestige pricing and price skimming is the intent and market

conditions. Price skimming is used to maximise return on investment in the shortest time by offering a new product variation to the market at the highest price innovators and early adopters are prepared to pay. When the market for the first price point is saturated, it is systematically dropped to a lower price point and the process repeated for as long as profitable.

In competitive, mature markets where there are already many competitors, for example, in the fast moving consumer goods market, at- or below-market pricing strategies are common. The simplest way to work out what to charge, subject to knowing the cost of production, is to follow the market and price within the consumers 'zone of tolerance' for the product. For commonly used products and services target consumers tend to have fixed internal price points as to what is acceptable. For example, toothpaste may be considered cheap at $2 but expensive at $5, with the average between $3 and $3.50 a tube. Price points will vary across the market and can be used as part of the segmentation strategy. Another example is haircuts, which can vary from $15 to $50 to $250 with each price point attracting a different market.

Pricing below the market, like pricing above, is governed by the positioning strategy. Sustained lower prices indicate a 'budget' brand, with perceptions of poorer but acceptable quality. Penetration pricing as a new product pricing tactic is useful in encouraging brand switching to trial the new product and to gain market share, but is a short-term sales promotion orientated approach which ultimately will lead to higher prices to match market expectations.

Place (distribution)

Distribution of the product can be:

- *exclusive*, which means being available in a single outlet per geographic region
- *selective*, which means being available in a distinct category of retail outlets (such as department stores or discount stores)
- *intensive*, which means being made available via the maximum possible number of outlets and using a combination of methods of delivery.

These three distribution approaches can be tied into product differentiation strategies where the product's relative competitive advantage is influenced by the accessibility of, or the social message incurred by, its distribution point. Similarly, distribution may also be a key to market development strategies (Chapter 8). The decision to make distribution exclusive, selective or intensive depends on three key factors:

- *power of the suppliers and distributors*, which is where the stakeholders' issues of the suppliers (Chapter 3) become an important factor, along with the organisation's relationship with its supply chains. It is possible for a distributor or supplier to pressure a new entrant into the market into an exclusive deal. In addition, where a competitor has used an encircling defensive strategy, the channels to the market may be blocked, and may required the development of a bypass, flanking or guerrilla distribution strategy.

- *power of the manufacturer*. Where the producer of the value offering is well established with a highly desired product, it can set terms as to how much access the public gets to the product.
- *characteristics of the product*, which is where the positioning of the product is enhanced through the distribution channel selection. For example, prestige products enhance their scarcity value by being available in only limited outlets whereas fast moving consumer goods look for broad distribution via a variety of retail outlets (including supermarkets, convenience stores and self-serve vending machines). This interconnects with growth strategies (Chapters 7–9) and product differentiation (Chapter 11).

When dealing with the specific case of services, the fundamental decision to be made is whether to take the service to the customer or expect the customer to come to the service. Again service characteristics will help determine the answer to this question. Pure services requiring little equipment are more able to come to the client, even though this is not always true. In contrast, where the client comes to the service, it is essential that the choice of location is consistent with the overall positioning strategy and complements the marketing mix.

Promotion (communication)

Promotion is the most visible part of the marketing process. It covers all forms of communication with consumers and stakeholders from mass advertising through to the development of personalised sales presentations. In the overall marketing plan the choice of promotional methods needs to be outlined and justified in the light of the firm's overall marketing objectives. The breadth of activity undertaken in promotion often results in the organisation developing additional focused plans to implement promotional activity. In particular, it is common to split off a sales plan at this point along with a separate advertising plan and public relations plan. Regardless of whether or not this occurs for management reasons, the overall marketing plan still needs to contain a summary of the proposed promotional activities and justify how these will assist in achieving the firm's marketing objectives. This element of the plan interacts with the value chain components of sales activity and marketing, along with the relative conceptual advantage aspect of product differentiation.

The key components of marketing communications are covered by the promotional mix plans:

- *advertising*, which is the mass market message that is paid for by the sponsor. Advertising allows large numbers of people to be reached effectively, and while expensive overall, is relatively cheap per person reached. Advertising objectives are expressed in terms of reach and frequency of exposure.
- *public relations*, which is a form of mass communication and refers to the publicity and other non-advertising-based mass communications which combine to create the overall image and perception of the organisation, its products and services.

Unlike advertising, public relations activities cannot be guaranteed placement in the mass media. Success is usually measured in terms of media exposure.

- *personal selling*, which refers to the one-on-one communications with potential customers undertaken by a firm's sales force. Separate sales plans are usually developed in order to track the performance of individual sales staff as well as allowing management to monitor success in different geographic regions. This ties directly to the human resources and sales effort aspects of the value chain, and to the employee stakeholders.
- *sponsorship*, which is when the firm aligns itself with an external body, often a sporting team, charity, cause or cultural event, to improve its image by leveraging off the attributes associated with the sponsored property. Performance measures for sponsorships tend to focus on a combination of incidental exposure (e.g. the amount of television coverage a logo receives incidental to the broadcast of a sporting event), plus recall of the brand by those attending or watching the event.
- *sales promotion*, which is a general term used to cover all other marketing communication activities designed to boost short-term sales but which are not covered by the previous categories. Sales promotion techniques include competitions, coupons, short-term price discounts and so on with success generally measured in short-term sales peaks.

Resource allocation and budgets

The implementation of the marketing strategy requires financial, non-financial and human resources. Without adequate financial support, the best thought-out strategies will fail. Central to this element of the marketing plan are various financial analyses, including the elements of the balanced scorecard (Chapter 4). It is this element of the marketing plan which will often determine whether or not the strategy will proceed. Marketers without a strong financial background should bring in expert assistance at this point, as the financial analyses will be reviewed at management and board level by accountants and finance officers.

Two of the basic analyses expected in this part of the plan are:

- *break-even analysis*, which determines how many products need to be sold at the recommended price points to ensure that the organisation covers its costs.
- *return on investment*, which calculates how much profit is anticipated should the sales targets be reached.

The depth of analysis and types of analyses required will be dependent upon the organisation's internal financial reporting requirements and expectations.

With respect specifically to the marketing budget, funding a new marketing strategy or extending an old one can be financed in a number of ways. If the strategy relates to a new product then the money to fund it must come from an alternative source in the company and should be treated as an investment. In this case the strategy would be funded by the

objective and task method, which systematically costs each activity and applies for funding based on this objective analysis. Most marketing plans arise out of existing programs and are based on formulae such as a percentage of sales to fund the marketing-specific component of the plan. In the case of a product in a highly competitive market, the organisation will tend to look externally and try to match the marketing activities of its rivals, thereby taking a more reactive approach to the marketing strategy and therefore the marketing budget.

Action plan

As the name implies, the action plan consolidates the information from the preceding section into a series of time-based points. The action plan should clearly identify:

- what specific tasks need to be undertaken
- the priority order in which these tasks need to be undertaken
- who is responsible
- when the tasks should be completed.

Within the action plan, key milestones for achievement are identified and timetabled. It is useful to present these in a single chart which shows when each action needs to start and when it is expected to finish. This enables simultaneous tasks to be clearly identified as well as the sequence for achieving different milestones where one action builds on the results of another. This is especially important in organisations where the implementation of the plan will take place across a number of different divisions.

Evaluation and control

This final section of the plan focuses on how well the organisation is keeping to the intended strategy, the effect of the implemented strategy on both competitors and the organisation and allows the organisation the flexibility to make adjustments as necessary. Marketing planning is an iterative and dynamic process. Once a marketing strategy or set of tactics has been implemented, inevitably it will cause a flow-on effect in the marketplace. Competitors will react and consequently it may be necessary to make adjustments to the intended strategy. Similarly, a tactic may not work as well as intended and again, this will result in adjustments. However, without a clear process of evaluation and control it is possible for these effects to go unnoticed in the short term, and culminate in significant unexpected consequences for the firm.

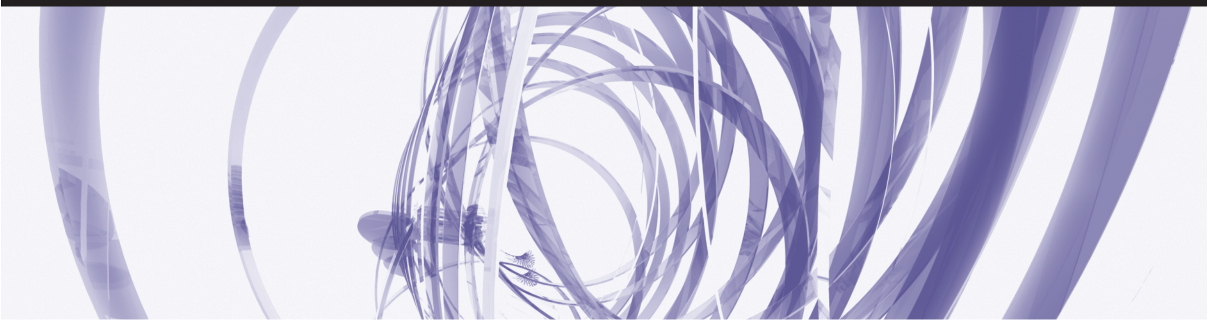
Within each plan there needs to be a clear set of metrics which demonstrate the impact of the plan. Chapter 15 discusses the concept of marketing metrics and reporting marketing outcomes in detail. When evaluating a marketing strategy and the effectiveness of a marketing plan, variations to the expected outcomes need to be analysed regardless of whether the unexpected variance was positive or negative. As part of the evaluation and control phase, a series of contingency plans need to be developed which outline the expected remedial actions to take should the initial strategy not result in the anticipated outcomes.

Conclusion

The tangible outcome of the marketing analyses and strategic decisions elaborated on in the preceding chapters is the marketing plan. While it is the process of marketing planning that steers the organisation in the right direction, it is the plan which encapsulates the decision-making processes along the way and provides a clear framework and guidance for organisational activities in the short- to medium-term. Strategic marketing plans are long-term and are intended to be relevant for periods of three to five years. Developing as an off-shoot of the strategic marketing plan are a variety of tactical marketing plans which are highly focused and intended to cover periods of approximately one year. These tactical marketing plans can focus on a specific target market, product or marketing function. In addition, the organisation can devolve the broader tactical plans into specialist plans to cover the implementation of specific elements of the marketing mix.

Implementing the marketing plan

CHAPTER 15



Introduction

This final chapter gives guidance on the practicalities of implementing a strategic marketing plan. It includes a discussion on resource acquisition and allocation so that the plan can be implemented within the confines of the firm's capabilities. It also gives an overview of marketing metrics and how to report on, and demonstrate, the value of marketing within the organisation.

There are four broad issues involved in implementing a marketing plan within an organisation:

- revising the goals of marketing
- establishing a market orientation
- implementing marketing metrics
- implementing the marketing plan.

Marketers may also need to deal with environments where marketing is unwelcome and unacceptable as a result of previous marketing failures, personality conflicts, or the organisation simply seeing marketing as an expensive waste of time. Consequently, marketers need to be mindful of how to operate in a non-marketing environment.

Marketing in the non-marketing firm

Not every organisation will want a market orientation, or even see a value in diverting resources towards marketing functions. In these environments, the marketing function has to assess what marketing outcomes are naturally occurring within the organisation, for example, an informal Kano Method process may arise during the sales negotiation for customer co-created products. Over time, and through demonstrable success in contributing to the organisation's bottom line, marketing can increase its role and involvement. However, marketers should not feel automatically entitled to internal organisational power on the basis of marketing theory. Simply because marketing textbooks espouse the value of marketing, and marketers who have degrees in the discipline see the inherent merit in its applications, this will not automatically grant organisational support. Marketing needs to demonstrate utility and value to the internal markets of the organisation, just as much as the organisation's value offering has to demonstrate utility to the consumer.

Revisiting the goals of marketing

Revisiting the fundamentals of marketing can assist different levels of the organisation to understand what is required to implement marketing within its limits and parameters. For the purpose of this chapter, the 2004 definition of marketing will be used to provide a framework for revisiting the goals of marketing. Within the definition, there are three functional areas that can be examined:

- *marketing as an organisational function and a set of processes*, which is where the priority is to establish marketing as an organisational function, and as a set of processes to be used in implementing the value offering. Marketing needs to be elevated from the advertising and promotion 'quick fix' status into a functional component of the organisation, alongside finance, accounting or human resources.
- *marketing's role in creating, communicating and delivering value to customers*, which is where marketing needs to be integrated across the value chain, and throughout the production process from concept development through to the actual delivery of the value offering to the customer. Integration should not be mistaken for total control—marketing needs to work with production, engineering, finance and other sections as part of an integrated approach. Dominating the creation, communication and delivery process without due consideration of the skills, insights and organisational knowledge of the other areas of the organisation will limit rather than enhance the success of the value offering. Marketing is only one facet of the organisation, and as such, while it can contribute its strengths in analysis, insight into the consumer and communications, it also has weaknesses and limitations that need to be covered by the strengths of areas such as finances, production or human resources.
- *marketing's role in managing customer relationships in ways that benefit the organisation and its stakeholders*. It is the responsibility of marketing to ensure that

it balances the needs of the market with the needs of the organisation. There is a risk that marketing can focus too heavily on the 'creation, communication and delivery of value' aspects, to the exclusion of managing the relationship for stakeholder and organisational benefit. Failure to manage relationships for benefit will damage the value of marketing's contribution to the organisation.

Managing relationships for benefit

One aspect of marketing's combined functional role and the relationship management for benefit requirement that has recurred consistently through the text has been the role of marketing in prioritising various aspects of the organisation's business strategies. Marketing's role in priority setting and ranking occurs in the following areas:

- *stakeholder analysis* (Chapter 3), where marketing's role is to set a strategic priority rank for each stakeholder based on their relative importance to the core business and mission of the organisation.
- *the Kano Method analysis* (Chapter 5), which involves marketing generating a prioritised list of features for the value offering sought by the customer.
- *prioritising objectives* (Chapters 6 and 14), which is where marketing's role involves determining which objectives will have the best chance of benefiting the organisation, and in which order these objectives should be implemented through the marketing plan.
- *customer retention* (Chapter 7), which is where the marketing orders the priority for converting retention into customer loyalty and long-term relationships for each customer group.
- *selecting market segments for market development* (Chapter 8), which is where marketing is involved in creating the ranking of marketing segments in order of their relative benefit to the organisation.
- *new product development* (Chapter 9), which is where marketing, in conjunction with the production section of the organisation, determines the relative production priority of the value offerings based on their value to the market, cost to produce and eventual benefit to the organisation.
- *defensive marketing strategies* (Chapter 13), which includes marketing's role in prioritising the markets, segments, niches and customers to retain through the use of the organisation's limited resources.

Establishing a market orientation

Kohli and Jaworski (1990) defined market orientation as the organisation-wide generation of, dissemination of and responsiveness to market intelligence. As marketing acts as an organisational functional area, it has a role in directing the organisation towards a market orientation. This requires the marketing function to establish the extent of the current market orientation in the organisation through a benchmarking process. This involves three steps:

- *benchmarking the current market orientation of the organisation*, which involves examining the extent to which the organisation is already orientated towards marketing practice and processes. This will assist the marketing function by being able to demonstrate internal functions that are consistent with the marketing process, even if the process is not internally recognised as being 'marketing'. For example, where an organisation has a strong customer focus through its interaction with the customers, this indicates a market orientation even if the organisation does not explicitly identify it as 'customer relationship marketing'.
- *aligning the organisation to the best-fit market orientation*, which is where the marketing function area attempts to align the organisation's internal processes towards a market orientation within the limits of the available resources and organisational tolerance.
- *refining and revising the marketing strategy*, which is where the marketing plan is adjusted based on the outcomes of the re-alignment, and the level of market orientation within the organisation.

Benchmarking market orientation

Market orientation can be both internal (focused on employees as customers) or external (customers as customers). Consequently, there are two baseline benchmarks of market orientation:

- external market orientation (Kohli & Jaworski 1990)
- internal market orientation (Lings & Greenley 2005).

External market orientation

Kohli and Jaworski (1990) saw the market orientation as the implementation of the marketing philosophy where the whole of organisation is orientated to servicing the needs of the market, rather than it being the responsibility of a single unit such as the marketing department. This was operationalised by Kohli and Jaworski as a three-factor market orientation scale (MARKOR). The MARKOR scale is based on three factors:

- *intelligence gathering*, which is the extent to which the organisation listens to the market through formal and informal processes. This connects to the internal (Chapter 4) and external analysis (Chapter 5), along with specific models such as Porter's (1985) industry analysis, and market research processes (Chapter 4). The intelligence gathering step involves examining the following areas:
  - current customer needs (Chapters 4, 7, 9 and 11)
  - needs of future customers (Chapters 5, 8, 9 and 11)
  - environmental influences on current and future customers (Chapters 3 and 5)
  - external environmental conditions of the market segment and industry (Chapters 2 and 5)
  - stakeholder needs (Chapter 3).

- *intelligence dissemination*, which is where the information gathered through informal and formal processes is shared through the organisation. Information sharing and dissemination is an assumed part of the systems component of the secondary value chain and as part of Day's (1994) organisational resource assets (Chapter 4).
- *responsiveness to the market*, which is the extent to which the organisation makes use of the information gathered and disseminated to influence marketing strategies (Chapters 7–13) and objectives (Chapter 6). This includes the incorporation of the information in the SWOT analysis of the marketing plan (Chapter 14) and the use of this information to assist decisions based on the Directional Policy Matrix (Chapter 2) or Porter's (1980) Five Forces Model. Overall, responsiveness to the market base can be seen as a key element of marketing strategies.

Within this text, external market orientation has been an assumption of the marketing strategies and tactics mentioned. Specifically, wherever Chapter 4 and Chapter 5 are mentioned in reference to a strategy, or as a source of information to inform a marketing model or process, this relates to the information gathering and dissemination elements. The use of this gathered information within the specific model is akin to the responsiveness component of the market orientation. Operationally, it is recommended that marketers conduct the MARKOR analysis on their organisation, either in a formal process or by using the Kohli and Jaworski (1990) scale as a list of potential marketing functionality.

Internal market orientation

Internal market orientation is the application of the Kohli and Jaworski (1990) market orientation to the internal business processes of the organisation, thus effectively using a marketing perspective for managing human resources (Lings & Greenley 2005).

An internal market orientation interconnects between the HR component of the value chain, and the employee, management and union stakeholders. In addition, it requires the reconceptualisation of the nature of the employee's role in the organisation as one of a customer who purchases a product or series of benefits (salary, working conditions) through exchanging their time, skills and abilities.

Lings and Greenley (2005) operationalised the internal market orientation construct around five key factors:

- *formal written information gathering processes*, which examine the formal written feedback from the employees, including questionnaires and job satisfaction surveys, written reports and other formal feedback processes.
- *formal face-to-face information gathering*, including formalised events such as meetings, interviews, appraisals and other open-ended formal discussion processes.
- *informal face-to-face information gathering*, which includes the management and employees' daily interactions that result in the exchange of information outside of a specific formal information collecting structure. For example, daily conversations on the factory floor between management and workers would result in information gathering.

- *information dissemination through formal and informal channels*, which is where the organisation collects, processes and then redistributes the information gained from the previous three steps.
- *responsiveness*, which is the extent to which the organisation uses the internally gathered information to improve working conditions, respond to employee needs regarding the organisation's value offering to the customer, and to enhance employee workplace satisfaction.

Internal market orientation can also be operationally tested through the use of measures in Lings and Greenley's (2005) article. Testing the internal market orientation of the organisation can assist the organisation in three ways.

First, where the organisation provides a service product as part of the value offering, the performance of the organisation's staff is a key influence on the customer's satisfaction. Various services marketing theories have demonstrated the interconnection between customer satisfaction and employee job satisfaction, where less satisfied employees were less likely to deliver high quality outcomes for the customer (Lings & Greenley 2005).

Second, the deliberate acquisition of employee-derived information feeds into both the internal market orientation processes and the internal analysis processes (Chapter 4). Employee knowledge is core to several areas within the strategic marketing process, including:

- the innovation component of Kaplan and Norton's (1996) balanced scorecard (Chapter 4), including the innovation objectives (Chapter 6).
- Day's (1994) organisational system assets, which included employee insight, experience and knowledge management systems (Chapter 4).
- market development strategies that rely on customer use innovations (Chapter 8).
- new product development based on employee innovativeness (Chapter 9).
- cost leadership based on employee learning, innovativeness and suggestions (Chapter 10).

Finally, the internal market orientation can have a positive impact on employee attitudes, employee motivation and the development of a positive working environment (Lings & Greenley 2005). Overall, engaging in the internal market orientation process should produce positive outcomes for value offerings that rely on a services component in the core, expected or augmented product. However, Stauss (1995) cautions that internal market orientation should augment rather than replace the external market orientation. The two areas should be seen as complementary approaches that can benefit the organisation by focusing value offerings on the target market whilst ensuring employee productivity and satisfaction.

Internal market orientation and the 2004 marketing definition

Although the original internal market orientation was conceptualised around the 1985 marketing definition, a modification of the 'employee as a customer, jobs as value offering' concept is possible. Under the 2004 definition, the internal market orientation would

involve the creation, communication and distribution of value (job) to customers (employees) and for a management–customer relationship (employee contracts and conditions) in ways that benefit the organisation (skills received, profitable outcomes) and its stakeholders (employees). Consequently, the internal market orientation under the 2004 definition allows for the management of the employee relationship for organisational benefit (profit, skills, value delivery to consumers) in parallel with managing the same relationship for the benefit of the employees amongst other stakeholders.

Aligning the organisation to a market orientation

Having assessed the organisation's combined internal and external market orientation through the use of MARKOR and internal market orientation scales, the marketing function can then adjust and where necessary realign the organisation to a market orientation. However, there are restrictions on realigning an organisation, including:

- *the resources of the firm*, which is the extent to which the organisation can afford to engage in best-practice market orientation, and the level of resourcing available to support information gathering, dissemination and responsiveness.
- *stakeholders' involvement*, which is the internal resistance to change that can be expected when the continuous to discontinuous innovation of market orientation is deployed through the organisation. Consider the use of the innovation adoption models (Chapters 2, 5 and 9) to assist in introducing the new concept to the stakeholders during internal marketing of the market orientation.
- *the organisational culture's attitude towards marketing*, which is where internal marketing is needed to understand the current internal market for the market orientation product. Where the organisation has had a poor track record of success with marketing, there is a strong likelihood of encountering internal resistance for the market orientation. In addition, understanding the organisational culture towards marketing can assist in developing internal positioning and product differentiation strategies to demonstrate the utility of the market orientation to the organisation.

In a perfect marketing world, the combined efforts of internal marketing and the improved organisational performance would result in the organisation adopting the market orientation in its entirety. In the reality of business, the market orientation is unlikely to be fully adopted due to a range of limitations of resources, stakeholder pressures, willingness to engage in marketing, and misunderstanding of the role of the marketing process and function.

Adjusting the marketing strategy

The final requirement of the market orientation is to adjust the marketing strategy to work within the available resources, frameworks and organisational culture. Market orientation can be won and lost on the basis of the performance of the marketing function. Adapting to the limited resources requires several factors, including:

- *expectation management*, where the marketing function accepts and specifies its own limitations, and works to reject the 'miracle maker' role within the firm. Many organisations see marketing as a repair process to use to solve the failure of a product. Whilst at times this role will have to be undertaken, reducing expectations that marketing can fix unsalvageable value offerings will assist in increasing the success rate of the overall marketing function.
- *insistence on accountability, metrics and measurement standards*, which is where the art side of marketing takes a back seat to the science side. Demonstrable contributions to the success of the firm, as measured through clear marketing metrics, will do more to increase the market orientation of the organisation than any internal marketing campaign. As illustrated in the balanced scorecard, financial objectives are the bottom line for the long-term survival of the firm. Demonstrating the contribution of marketing to the financial outcomes will assist in creating an ongoing marketing orientation.
- *limit marketing involvement to where it can contribute in a measurable capacity*, which is where the marketing function in a non-market-orientated organisation needs to ensure it stays focused on specific, measurable and deliverable outcomes that demonstrate its contribution to the organisation.
- *gaining support from other elements of the organisation*, which is where the market orientation can be increased by working with related aspects of the organisation, such as research and development, production or finance, in order to improve their outcomes with the assistance rather than direction of marketing.

Overall, marketing plans cannot be implemented without the support of key internal stakeholders in the production context. In the absence of implementation, there is little value to the planning elements of the marketing function.

Implementing marketing metrics

Marketing metrics are quantifiable standards to measure specific marketing outcomes (Wood 2004). They represent the introduction of increased levels of accountability, measurability and scientific method into the marketing function. In addition, marketing metrics are a valuable aspect of the marketing function which allow it to demonstrate its contribution to the organisation in a specific manner, rather than relying on broad statements of 'enhanced awareness' or 'improved attitudes towards the brand'. Within marketing metrics, there are three areas to address, including:

- metric selection
- the Australian Marketing Institute marketing metrics program
- Shared principles of metrics and objectives setting.

Overall, all aspects of marketing metrics are dependent on the ability of the organisation to establish preliminary benchmarks which are then measured for evidence of change.

For example, if an organisation cannot establish the pre-implementation levels of market awareness, it cannot use a market metric that measures market awareness. Metrics are based on the fundamental assumption that an existing benchmark measure will be remeasured to test for differences that should have arisen from the implementation of the marketing program.

Metric selection

Wood (2004) defines the process for selecting marketing metrics as a five-part model.

- Metrics must match the objectives of the marketing plan, marketing program and organisational objectives.
- Metrics should measure activities that show progress towards the organisational mission, goals and outcomes that are supported by the marketing activities.
- Metrics must measure non-financial and financial measures which are quantifiable, and which are relevant to the organisation, stakeholders and customer outcomes.
- Metrics should include relevant internal and external outcomes. Internal metrics address factors such as product quality and production errors. External measurements include market share, customer satisfaction and other outcome-based measures.
- Metrics should provide sufficient information to support the ongoing priorities and objectives of the organisation.

The Australian Marketing Institute marketing metrics program

The Australian Marketing Institute (AMI) has undertaken the development of a set of national marketing metrics standards based on the work of Ambler (2003) and others. Whilst metrics are diverse, and each organisation will have its own requirements, the AMI recommend four core metric elements. These are:

- *return on marketing investment*, which is the return on investment and economic value added to the organisation from the expenditure on marketing activities. This ties to the Kaplan and Norton (1996) financial objectives element of the balanced scorecard (Chapter 4).
- *customer satisfaction*, which is the extent to which the organisation is meeting the needs of the customer, and the customer's intention to continue using the organisation's value offering. This is linked to Kaplan and Norton (1996) customer relationships element of the balanced scorecard, core customer outcomes (Chapter 4), customer relationship objectives (Chapter 6), and the various measures of customer satisfaction within the growth strategies (Chapters 7–9) and value addition strategies (Chapters 10–12).
- *market share in targeted segments*, which is the volume of the market controlled by the organisation as a percentage of the total market. Market share metrics are one

of the primary measurements of the success of growth strategies (Chapters 7–9) and are also used in a range of strategic decision-making models (Chapter 2).
- *brand equity*, which is how the brand stands out in the marketplace (Ambler 2003). This measures the relative conceptual advantage held by the organisation's marketing communications (Chapter 11), and ties into the broad image and reputation of the organisation (Chapter 4).

As can be seen by the backwards referencing to other chapters within the text, several of the component elements of these marketing metrics have are already been discussed and are regarded as vital aspects of marketing strategy. For example, understanding the share of the market is core to the decision-making models (Chapter 2) and objective setting (Chapter 6). Further, it influences core offensive and defensive decisions such as either electing to dominate a market in response to market decline or deciding to sacrifice smaller markets in a contraction defence tactic. Quite frequently, organisations already have collected much of the information required for these core metrics. In addition to these core metrics standards, the AMI endorses the use of metric clusters, which are based on four areas:

- financial metrics
- brand equity metrics
- innovation metrics
- employee metrics.

The AMI metric clusters are based in part on three of Ambler's (2003) metric groups, with the addition of the financial metric. These are examined in depth in the following sections.

Metric cluster 1: financial metrics

Financial metrics are those measures based on changes in dollar values resulting from marketing activities, and include:

- *sales*, which are measured by volume, dollar value or market share. This information should be captured by the organisation as part of day-to-day business. From a marketing perspective, this influences the financial analysis component of the internal analysis (Chapter 4), and the finance objectives of the balanced scorecard. It measures the impact of the sales effort of the primary value chain and the results of the growth and value addition strategies (Chapters 7–12). It also forms the basis for determining defensive strategies, such as the rate of sales decline, and sales return from harvest strategies (Chapter 13).
- *marketing investment*, which is the financial measure of the costs of the ongoing integrated marketing communications process which is measured by the period costs (expenditure for voice) and the share of voice, which is the effectiveness of that expenditure. Share of voice has previously been defined as the ability of the stakeholder to speak freely (Chapter 3). In this case, it represents the level of

competition in the marketplace for the organisation's brand message, and/or the extent to which the organisation can freely communicate the value offering to the market. Measurement of marketing investment outcomes forms part of external analysis (Chapter 5), forms part of relative conceptual advantage (Chapter 11), and ties into the marketing objectives (Chapter 6).

- *bottom line*, which is the overall profitability of each product line, and its contribution to the profitability of the organisation. This is measured in per-unit margin, profit, share of profits and other accounting measures. Part of the information gathered for this metric can be used in cost leadership strategies (Chapter 9), defensive marketing decisions with reference to harvest and divestment strategies (Chapter 13), and financial components of the internal analysis (Chapter 4). It has a direct relationship to the financial objectives of the balanced scorecard and the portfolio analysis (Chapter 6). This metric is often of most interest to the board of directors, shareholders and creditor and financier stakeholders.

Metric cluster 2: brand equity metrics

The second metric cluster is based on Ambler's (2003) brand equity metric, and is part of the AMI's core metric group. Brand equity was defined as how the brand stands out in the marketplace across six metrics:

- *familiarity*, which is measured by the extent to which the consumer is familiar with the organisation's brand when compared to related competitor brands. This is related to the personality niche concept (Chapter 12), the communication of value to the consumer (Chapter 1), market potential and market advantage (Chapter 5), market development (Chapter 8) and financial analysis in new product development (Chapter 9).
- *penetration*, which is the number of customers the organisation has within the niche, segment or market. Knowledge of the size of the organisation's share of the market underpins all three growth strategies (Chapters 7–9), along with the financial metric of sales.
- *brand perception*, which relates to the consumer's perception of the quality of the product and its relative competitive advantage over the competitors. This type of metric assists with product development (Chapter 9) and product differentiation strategies (Chapter 11). In addition, this information is captured as part of the customer analysis (Chapter 5) and core customer outcomes (Chapter 4).
- *feelings about the brand*, which is the consumer's attitudes to the brand, the social message conveyed by the organisation's brand, and attitudes towards the image of the organisation. This metric measures the relative conceptual advantage of the firm (Chapter 11), and ties closely into branding, product differentiation (Chapter 11) and personality niches (Chapter 12).
- *loyalty*, which is measured by behavioural components of repeat purchase, membership of relationship marketing schemes or other appropriate metrics for the

value offering. The loyalty metric encompasses the dual components of retention and loyalty from market penetration (Chapter 7), along with elements of core customer outcomes from the internal analysis (Chapter 4). Loyalty underpins most aspects of the growth, niche and defensive strategies that require a core group of non-price sensitive customers (Chapters 7–13).

- *availability*, which is the marketing metric that covers the delivery of value to consumers, and encompasses the reporting of the success of the distribution element of the marketing mix. Distribution is a measure of the effectiveness of the delivery of the value offering and is incorporated into market potential (Chapter 5), market development (Chapter 8), and product differentiation (Chapter 11).

The brand equity metrics encompass the broad areas of relative competitive advantage (Chapter 11), and the success levels of the implementation of the marketing mix in creating, communicating and delivering value to the customer (Chapter 1).

Metric cluster 3: innovation metrics

The third level of metrics is the innovation defined by Ambler (2003) as management-inspired changes that alter the organisation's position in the market. Consequently, the innovation metric will measure outcomes associated with product development (Chapter 9), market development (Chapter 8) and product differentiation (Chapter 11). These strategies are connected to the innovation objectives (Chapter 6), and the organisational innovation components of the balanced scorecard (Chapter 4). Ambler (2003) outlines three areas of innovation metrics:

- *strategy*, which is represented by internal analysis of the organisation's leadership, positioning, goal setting and resource allocation. As with most metrics, this requires individualised custom measurements for the organisation to assess and analyse the levels of support allocated by the organisation to the marketing process.
- *culture*, which is a mixture of measuring the market orientation of the organisation, along with the presence or absence of cultural facets such as tolerance of failure and the learning aspects of the balanced scorecard's innovation component.
- *outcomes*, which is a measure proposed by the AMI that examines the revenue from innovation, number of new ventures, level of innovativeness measured by new product development (Chapter 9), market development (Chapter 8) or modifications to product offerings (Chapter 11). It can also include changes to internal product processes including modifications to the primary and secondary value chain (Chapter 4) or the implementation of cost leadership (Chapter 10).

Metric cluster 4: employee metrics

The final aspect is the employee metric, which measures the level of internal satisfaction, and is interconnected to the internal market orientation (Ambler 2003). In essence, the employee metrics report on the preconditions and outcomes of the internal market orientation process, and address the following areas:

- *familiarity with the organisation's objectives and goals*, which is the extent to which the aims of the organisation have been successfully communicated and marketed to the internal audience of employees.
- *brand issues*, which is the employee's perception of the relative advantage or disadvantage incurred by working for the organisation.
- *organisational loyalty*, which is the employee's intention to remain with the organisation, and is partly tied to their perception of the organisation as a brand, and their perception of the benefit they receive in exchange for their skills, time and effort.

Overall, the employee metrics are closely related to, and should be derived from, the organisation's employee stakeholder issues. Understanding the employees' needs and setting metrics to ensure these are met is consistent with the internal market orientation.

Table 15.1 outlines a summary of the interaction between the marketing metrics and their related objectives from Chapter 6.

TABLE 15.1 Metrics and objectives

Metric cluster	Metrics	Objectives
Financial	Bottom line	Financial
	Marketing investment	Financial
		Marketing
	Sales	Customer relationship
		Financial
		Marketing
Brand equity	Familiarity	Marketing
	Penetration	Customer relationship
		Financial
		Marketing
	Brand perception	Customer relationship
		Innovation
		Marketing
	Feelings about the brand	Customer relationship
		Internal business
		Marketing
		Operational
		Social/societal
	Loyalty	Customer relationship
		Marketing
	Availability	Marketing

continued

TABLE 15.1 **Metrics and objectives (cont.)**

Metric cluster	Metrics	Objectives
Innovation	Strategy	Innovation
		Internal business
		Marketing
		Operational
	Culture	Innovation
		Internal business
		Operational
	Outcomes	Financial
		Innovation
		Internal business
Employee-based	Familiarity	Internal business
		Operational
	Brand issues	Operational
	Organisational loyalty	Operational

Tying metrics to objectives: shared principles for metric and objective setting

Setting organisational objectives involved a series of criteria outlined by Cohen (2001), Wood (2004) and Viljoen and Dann (2003) in Chapter 6. As the role of the marketing metrics is to demonstrate the success (or otherwise) of marketing objectives, metrics are also influenced by the principles associated with objective setting. These principles include:

- *acceptability*, which is the acceptance of the metric by key stakeholders such as the employee, management, board of directors or shareholders. If a stakeholder rejects the acceptability of a metric, then there is no value in reporting on that marketing outcome to this stakeholder. For example, whilst management and employees regard brand equity as important, shareholders may dismiss it in favour of sales outcome measures. Consequently, when reporting marketing metrics to the shareholders, it is important to report those measures that are accepted by that audience and leave out the rejected measures.
- *feasibility*, which is the extent to which the objectives can be measured by the associated metric, and the information required for the metric can be captured. For example, an innovation metric can measure the number of new product concepts that are put through the new product development process in a year, as it will be feasible to track this. A metric to determine the financial costs associated with not implementing a rejected product idea is not one that can be feasibly measured.

- *flexibility*, which is the level to which the objective can be adjusted to reflect changed market conditions. If the objective changes, the measurement of its outcome has to be able to be adjusted to the new conditions. Inflexible metrics can measure the wrong information, for example, if the organisation has engaged a defensive strategy to consolidate market share instead of pursuing growth, maintaining customer retention levels is the sign of a successful defence. If the metric is still focused on growth, rather than the appropriate metric of maintenance, the information collected will at best be inaccurate, and at worst, be misleading.
- *commitment-inducing*, which is the level to which the objective is supported by other members of the organisation, both at the employee and managerial levels. Whilst metrics do not need to induce commitment, they do need to be supported by the employees and management groups responsible for collecting the information.
- *linked to organisational principles*, which is the extent to which the objectives are able to be traced back to the organisation's overall direction, principles and long-term goals. Similarly, Wood (2004) illustrated that the metrics selected should measure progress toward longer-term objectives, goals and outcomes.
- *measurability*, which is the level to which the activities leading to the completion of the objective can be observed, measured and reported over a period of time. Understandably, every metric selected by the organisation must be able to be quantified or otherwise measured. This also encompasses the critical requirement that a benchmark measure be undertaken before the marketing campaign is implemented so that any differences can be measured.
- *motivating*, which is the level to which the goal provides direction and drive for those people working to achieve it, and to which the measurement of this goal does not interfere with the motivation to achieve it.
- *participative*, which is the extent to which those involved in the implementation of the objectives have a say in the creation of those objectives and how they will be measured. Employee involvement in the marketing metrics is an important factor in ensuring the metrics are collected.
- *suitability*, which is the extent to which the objective matches the organisation's basic purpose and reason for existence, and the metric matches the objectives. The information collected by the metric should only be used for measuring the outcome the metric is associated with, and should not be used as the basis for other measures. For example, customer satisfaction with the availability of employees should not be used as a surrogate measure to determine if the organisation can reduce its staffing levels.
- *understandable*, which is the extent to which the objective can be interpreted and understood correctly and consistently by all stakeholders. Similarly, metrics need to provide information rather than raw data. This requires the metrics to be used as part of an analysis process where the information collected is presented in an understandable way for the relevant stakeholders.

Implementing the marketing plan

Implementing the marketing plan involves engaging in the tactical and operational level decision making regarding how to best communicate the value offering and the positioning of the organisation in the market. This incorporates:

- *resource allocation*, which is where the organisation allocates its limited time, finances, capital, production processes and human resources to the marketing plan.
- *control*, which is where the organisation uses marketing metrics to assess the ongoing success or failure of the plan, strategy or product.

Resource allocation

Resource allocation is inherently based on the capacities of the organisation (Chapter 4), industry conditions (Chapter 5), strengths of the organisation, human resource capacity of the value chain (Chapter 4) and the production context stakeholders. It also represents the last application of the truism of marketing strategy, that the shorter sections in the text relate to the longest processes in practice. Resource allocation has been mentioned previously in:

- dealing with stakeholder issues and, more specifically, as a role for the board of directors and managers (Chapter 3)
- shareholder value (Chapter 4)
- marketing plans (Chapter 14).

Overall, organisation resource allocation is usually a negotiated process that requires the justification of expenditure and defence of budget proposals. This is supported by the presence of marketing plans that demonstrate how the organisation intends to use the resources, and marketing metrics that demonstrate the return for the organisation on previously allocated resources.

Control

Best (2005) outlined the control aspect of marketing as being a three-part process of ownership, support and adaptation. Ownership incorporated the internal marketing processes, which create:

- *detailed action plans*, which quantify what needs to be done, by which section of the organisation, by what date and which metric would be used to assess the outcome
- *management of the process and action plan*, which specifies the managerial aspect of who is responsible for the implementation of the plan, and which members of the organisation are part of the ownership team that implements the action plan
- *compensation*, which indicates the rewards for implementing the plan or being part of the ownership team, which includes the employee's salary plus additional value offerings that enhance motivation and responsibility for outcomes

- *involvement of management*, which includes the stakeholder issues of the managerial level in ensuring the employee stakeholders deliver the promised outcomes, and issues associated with how the managerial level staff can assist or support the action plan's implementation.

Support for the marketing plan incorporates both managerial ownership and involvement, along with the allocation of resources. Specifically, Best (2005) also included the following factors:

- *time to succeed*, which is where the organisation supports a plan for a reasonable length of time, and does not expect immediate outcomes from long-term processes. This also relates to the concept of the marketing metrics measuring progress towards an organisational outcome, rather than only focusing on short-term sales or revenue figures.
- *resource allocation*, which was mentioned previously in this chapter and includes the provision of money, human resources, organisational support and access to the requisite elements of the value chain (such as the production processes or research and development).
- *communications*, which is where the organisation acts on the communication of value aspect of the marketing definition. This factor incorporates internal marketing communications that can be measured through the employee-based metrics, along with external communications issues. External communication includes ensuring the value offering is communicated to the following groups:
  - *target customers*, who are the primary purchasers of the value offering.
  - *channel intermediaries*, who are the distributor stakeholders who need to be aware of the product, its features and likely market demand in order for them to distribute the value offering to the retailers and consumers.
  - *trade press*, which is the communicator of market signals through industry-specific trade magazines.
  - *market influencers*, who are those members of a market such as the critics, magazine editors, reviewers, consultants or other people who will recommend the organisation's value offering to target customers.
  - *broader media*, used for public relations and publicity to augment the integrated marketing communications that communicate with target audiences.
- *required skills*, which is where the organisation either acquires, retains or trains employees with the skills necessary for the implementation of the marketing plan.

Finally, control also involves the adaptation of the marketing plan as market conditions change and evolve. As noted elsewhere in the book, markets are not static environments, and the introduction of the organisation's product will be met by a reaction from competitors and the market. Consequently, the conditions under which the original plan was designed will change, and the changed conditions need to be incorporated into the activities of the organisation. This is also emphasised in the need for objectives and metrics

to be flexible to adapt to changed conditions. Best (2005) highlights four elements of adaptive control:

- *continuous improvement*, which is where the company incorporates changes to the conditions of the market as part of the operation of the plan. For example, a product differentiation strategy may require constant alteration as the point of differentiation is copied by competitors or becomes part of the expected product (Chapter 11).
- *feedback mechanisms*, which is the ongoing use of the marketing metrics, customer feedback, knowledge management systems, internal and external analysis to maintain an ongoing awareness of the market conditions.
- *persistence*, which is the organisational willingness to accept failure as part of the process of success. Organisations which expect to be successful first time, every time usually end up failing due to unrealistic expectations, or because the organisational culture becomes focused on meeting internal metrics rather than satisfying customer needs.
- *adaptive roll-out*, which is the ongoing pursuit of the overarching organisational goal or objective coupled with the willingness to alter the methods used to reach the end game. This relates to both the flexibility and the time to succeed as the original design for the value offering may need to be altered numerous times in pursuit of the final successful outcome of growth or cost leadership.

Conclusion

Chapter 15 examined four broad issues involved in implementing a marketing plan within an organisation. First, it explored the revision of the goals of marketing as part of the process of ensuring the capacity to create, communicate and deliver a value offering to a customer for the benefit of the organisation and its stakeholders. Second, the chapter overviewed the use of the market orientation as a means to improve the marketing outcomes of the organisation. This included the dual use of internal and external market orientation measures, along with the steps necessary to align an organisation toward a market orientation. Third, marketing metrics were discussed in terms of their value to marketing, the organisation and the type of metrics that can be used to measure marketing outcomes. Finally, issues of implementation and control were examined, including resource allocation for the marketing plan, and the use of metrics as part of the control function.

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CHAPTER 16

Introduction

The American Marketing Association (AMA) definition of marketing changed within the first twelve months of Competitive Marketing Strategy's shelf life. As the CMS text is built on the core platform of the 2004 definition of marketing, the text requires an update. In the time honoured tradition and best practice of Microsoft, Apple, and software developers everywhere, the authors are issuing this chapter as an interim patch whilst Competitive Marketing Strategy 2.0 is developed.

The 2004 AMA definition was "marketing is an organizational function and a set of processes for creating, communicating and delivering value to customers and for managing customer relationships in ways that benefit the organization and its stakeholders". Following significant criticism amongst the marketing and academic communities, this has now been modified to

> "marketing is the activity, set of institutions and processes for creating, communicating, delivering, and exchanging offerings that have value for customers, clients, partners, and society at large."

The summary of changes between AMA (2004) and AMA (2007) are as follows:

- Marketing has changed focus from "organisational function" to "activities, processes and functions", and moved away from the previous role of creating benefit for the organisation (AMA 2005) and satisfying organisational goals (AMA 1985) to "exchanging offerings that have value for customers, clients, partners and society at large."

- Exchange theory has been reintegrated into the definition with an expanded role in the marketing process alongside creation, communication and delivery of value.
- The outputs of the marketing process are now "offerings that have value" rather than value itself in recognition of the role of the consumer in the creation of value
- Management of customer relationships for organisational benefit has been relegated to the sidelines due to the interpretation of "managing relationships with customers" as the tactical element of CRM, database marketing rather than the Gronroos (1994) conceptualisation of relationship marketing
- The targets of the outcomes of the marketing process have changed from customers, organisation and stakeholders to four distinct groups of "customers, clients, partners and society at large". Clients are recognised as the recipients of non-commercial marketing, and partners are seen as those involved in the organisation and its value chain

Exploring the AMA (2007) definition of marketing

The definition of marketing can be viewed as a holistic model of the nature of marketing, or a composition of component elements that can inform the view of marketing, but not limit it to the parameters of the definition. A definition can be interpreted as exclusive wherein anything that is not defined as part of the whole is excluded, or can only be added through future interpretation of component elements. Alternatively, a definition can have an inclusive reading whereby anything that can reasonably be read into the definition through the interpretation of both the literal meaning of the words and intention of the definition is fair game for inclusion.

For the purposes of this chapter, the AMA (2007) definition is being read as an inclusive definition whereby aspects of marketing that can be reasonably interpreted as belonging to the definition are implicitly included. However, by interpreting the definition in this manner, the text is providing a wider reading of the definition than may have been intended by the authors. Further, the chapter also explores several of the limitations of the new definition that are caused by either a narrow reading of it as an exclusive definition, or where the definition relies on assumed knowledge that would not be reasonable for a newcomer to marketing to know in order to interpret the definition. The definition of marketing has been divided into three sections for the purposes of interpretation

- the activity, set of institutions and processes
- Creating, communicating, delivering and exchanging offerings that have value
- Customers, Clients, Partners and Society

These changes between the AMA (2004) and the AMA (2007) brought about by these four elements will be examined later in the chapter.

Activity, set of institutions, and processes

The first aspect of the AMA (2007) definition of marketing is the broad inclusion of the possible means by which marketing can be conducted as an activity, set of institutions, and processes. This is similar to the division of marketing as a business philosophy, strategic framework and series of tactical measures (Chapter 1). In following this analogy, the marketing activities are closest to the tactical implementation level, including the objective setting (Chapter 6), marketing planning (Chapter 14), decision making and implementation activities (Chapter 15).

Marketing as a set of institutions has the less clear cut compatibility with the philosophy of marketing, unless the "set of institutions" is interpreted as included aspects such as market orientation, customer focus and other philosophical frameworks of marketing as institutions of the organization. Alternatively, the "set of institutions" aspect can be interpreted as the more mundane level of marketing departments, organizational functions, and the presence of marketing within the Porter Value Chain model (Chapter 4 and Chapter 5).

Marketing processes are the strategic frameworks which connect the marketing tactics with the philosophy of customer orientation (chapter 1). This can also include the processes such as the internal analysis (chapter 4), external analysis (chapter 4), and strategic behaviors such as market development (Chapter 7) or new product development (Chapter 9). Similarly, other procedural aspects of marketing can be incorporated into the "processes for creating, communicating, delivering and exchanging value".

Creating, Communicating, Delivering, and Exchanging Offerings of Value

This aspect of the AMA (2007) is the closest to the AMA (2004) definition, and as such, inherits much of the features of the previous definition. Product, promotion and distribution are represented explicitly as key elements of the process, institution and/or activities of marketing. As with AMA (2004), price is again absent from any form of explicit recognition, and is implied as part of the marketing process of "exchanging offerings that have value".

The exclusion of price as an formal role of marketing presents a complex problem for marketers – at the theoretical, conceptual and ideal level, price is used as both a revenue source and communications tool. In reality, price was more likely to be set by the finances of the organization rather than by the marketer. That said, many marketers also find themselves without a role to play in product development, yet creation of offerings of value remains a marketing role, and price has been subsumed into the creation, communication, delivery and exchange of offerings of value. The AMA (2007) definition also recognizes that whilst value is created by the customer, it is created in conjunction with the offer from the organization. Consequently, marketing implicitly recognizes the role of ideas, goods and services as offers which can be used by the consumer to co-create value. Use of value as a metric of exchange also allows marketing to lay claim over exchanges that involve non-monetary exchange such as brand development, goodwill, awareness, or creation of social meanings associated with the organization's offerings. This is explored further later in the chapter.

Customers, clients, partners, and society at large.

The marketing efforts of the organization are now targeted towards the providing commercial offerings of value to customers or, alternatively, non commercial offerings to clients, whilst also dealing with the flow of exchange between partners and society. The AMA divided the role of the consumer between the recipients of for-profit and not-for-profit activities based on understanding that the term "customer" was too limited to describe the non-commercial applications of marketing.

The term "clients" has been introduced to specifically refer to those beneficiaries of market offerings who are not customers in the traditional sense (e.g. money for goods/services). In this context, the term 'clients' is referring to the recipients of non commercial applications of marketing. Effectively, from a competitive marketing strategy perspective both clients and customers are similar in nature insofar as they are the customer stakeholders in the consumption process.

"Partners" creates a grey area within the definition as to where the organisation sits in terms of receiving value from the marketing process – for the purposes of this chapter, partners includes the organisation and the production context stakeholders. In the preliminary draft of the AMA (2007) definition (see boxed vignette), the term "marketers" was included to replace the AMA (2004) concept of benefit to the organisation. Given that "marketers" was replaced by the broader term "partners", which can include suppliers, distributors, wholesalers and other participants in the marketing process, the term will also be taken to represent the marketing organisation in the new definition.

"Society at large" represents the incorporation of the principles of benefit for stakeholders into the AMA (2007) definition by including the regulation context and environment context stakeholders. The exploration of the role of the four target groups and the stakeholder holder framework is examined in greater detail later in the chapter.

Development of the AMA Definitions

The historical development of the AMA definition is an important factor in understanding how the contemporary definition has incorporated or excluded functions associated with the previous definitions. Table 1 outlines each marketing definition, broken down into component parts, and where these parts match across the evolution of the definition of marketing from 1935 to 2007.

The visual map of the definitions highlights three points explored in depth below. First, between 1935 and 2004, the definition shifted away from an emphasis on organisational outputs of ideas, goods and services and towards the consumer input of "value". In 2007, these outputs were once again recognised as the means by which the market could access "value" being created, communicated, delivered and exchanged. Second, the 2007 definition does not have a clear line of connection with the concepts of organisational benefit or organisational objectives. Finally, the recipients of marketing have been expanded from consumers through to the customers, clients, partner and the whole society as marketing recognises its capacity as both a business tool and a societal influence.

TABLE 16.1

Table 1: American Marketing Association Definitions over time

AMA (1935)	AMA (1985)	AMA (2004)	AMA (2007)
marketing is the performance of business activities that direct the flow of goods and services from producers to consumers	marketing is the process of planning and executing the conception, pricing, promotion, and distribution of ideas, goods, and services to create exchanges that satisfy individual and organizational objectives	marketing is an organizational function and a set of processes for creating, communicating and delivering value to customers and for managing customer relationships in ways that benefit the organization and its stakeholders	marketing is the activity, set of institutions and processes for creating, communicating, delivering, and exchanging offerings that have value for customers, clients, partners, and society at large
		an organizational function	
the performance of			the activity
business activities	process of planning and executing	a set of processes for	set of institutions and processes
	conception	creating	creating,
	pricing		
	promotion	communicating	communicating
direct the flow	distribution	delivering	delivering
	to create exchanges		exchanging
goods and services	ideas, goods, and services	value	offerings that have value for
		managing customer relationships	
from producers	organisational objectives	benefit the organization	
to consumers	individual objectives	value to customers	customers
		and its stakeholders	clients
			partners
			society at large

A brief refresher on AMA 2004

In 2004, after a period of public consultation, the AMA redefined of marketing as

> "an organizational function and a set of processes for creating, communicating and delivering value to customers and for managing customer relationships in ways that benefit the organization and its stakeholders.

Three issues need to be noted regarding the 2004 definition of marketing. First, this definition represents the largest, and most radical conceptual shift between marketing definitions. Changes in between the 1935 and 1985 definition were comparatively incremental as marketing moved from "goods and services" to "goods and services and ideas". In contrast, the AMA (2004) definition replaces the product offerings of goods, services and ideas with the customer created notion of "value". Although value is undefined within the context of the definition, it is generally accepted to be the bundle of intangible benefits that the consumer derives from ownership and use of the marketer's product offering.

The substitution of the "goods, services and ideas" can be attributed to the rise of value based marketing which was reflected in Vargo and Lusch's (2004) service dominant logic framework, and the Dev and Schultz (2004) alternative marketing mix. Service dominant logic regards marketing as a means of service delivery where the value is co-created by the customer engaging in

- internally administered self service through the adoption and use of idea products
- assisted service whereby the customer is the recipient of a traditional service encounter, or
- the use of an embedded services through the consumption of physical goods

Second, the AMA (2004) definition attempted to shift away from a transactional focus and into the long term management of the relationship between the organisation and the customer. However, "managing customer relationships in ways that benefit the organisation" was not universally interpreted by marketing academics or practitioners. The division arose between the interpretation of "managing customer relationships" as either the tactical level implementation of database driven, direct marketing orientated, customer relationship marketing, or alternatively as the recognition of Grönroos (1994) and the Nordic school of relationship marketing.

Third, the AMA (2004) definition also presented an alternative view of the marketing concept as a set of processes for "creating, communicating and delivering value". In the context of the role and purpose of marketing, "creating" incorporated the AMA (1985) "conception", "communicating" was interpreted to represent promotion, "delivering" incorporated distribution and pricing, and "value" was extended to include "ideas, goods, services". This was seen as replacing the exchange concept based on mutually beneficial outcomes for organisation and consumer with an organisation sided approach to marketing whereby the organisation created, communicated and delivered a value offering to a managed relationship with the customer predominantly or exclusively for the benefit of the organisation. Value and benefit were treated as separate concepts which reduced any formal recognition of the exchange concept within the definition of marketing.

AMA 2007

The 2007 definition was developed as a response to the criticisms of the AMA (2004) by academic and practitioner members of the American Marketing Association. The revised definition describes marketing as:

> "the activity, set of institutions and processes for creating, communicating, delivering, and exchanging offerings that have value for customers, clients, partners, and society at large."

The AMA (2007) definition conceptualises marketing as a three part system of "activities, institutions and processes" which in turn are seen as the mechanisms for creating, communicating, delivering and exchanging offerings of value. Stakeholder benefit's inclusion was short-lived as this aspect has been subsumed into a broad statement of "value

for customers, clients, partners and society at large" framework. The AMA (2007) definition has removed the dichotomy of "benefit and value" to emphasize shared value between market and marketer where the actions of the marketer should be beneficial to the market place (customer/clients) broader community including the stakeholders (society at large).

The Changes between AMA 2004 and AMA 2007

There are five distinct areas that have changed in the 2007 definition compared to AMA (2004). These are the change of focus, the return of exchange, altered understanding of the outputs of the marketing process, the end of the brief role of customer relationship management, and the clarification of the targets of the marketing activities, processes and institutions.

Changing the focus of marketing

The first significant change between AMA (2004) and AMA (2007) is the redefinition of marketing as an activity, set of institutions and processes rather than as a functional component of a larger business process. This change increases the range of activities that can be encompassed by the marketing definition to include entrepreneurial behaviours by individuals, firms, non profit, government and social institutions. As an activity, marketing is found when the activity is undertaken, institutions exist or the processes are being used rather than needing a recognised organisational function.

In addition, recasting marketing as an active force rather than a formal function merges the AMA (2004) "set of processes" with the recognition of the reality of marketing in organisations as activities (eg marketing campaigns), sets of institutions (eg marketing department) and processes (eg implementation through sales etc). This aspect of the marketing definition recognises the split responsibility held by marketing in Porter's (1985) value chain with the processes and activities reflected in the primary value chain (sales) and the sets of institutions are explicitly mentioned in marketing's role in the secondary value chain (Chapter 4).

Organisational objectives, organisational benefit and the new definition

Noticeable by its absence in the AMA (2007) definition is the concept of organisational benefit and/or direct and mutual gain for the organisation which has been a factor in the formal marketing definition since 1985. Previous definitions of marketing have been explicit in recognising its role and purpose as a means to meet organisational objectives or to create benefit for the organisation.

Potentially, the most controversial change between AMA 2004 and AMA 2007 is the removal of any explicit recognition of direct benefit to the marketing organisation. Whilst AMA 2004 was criticised for the overemphasis on direct benefit to the exclusion of sub disciplinary areas of marketing dependent on indirect benefit (Dann, 2005), this definition has reversed the trend to the other extreme. Whilst the interpretation of the definition of "partners" as the production context stakeholders allows for the flow of "offerings that have value" to the organisation via the stakeholders proxies, there is no direct role of marketing

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as a means to meet organisational objectives under the AMA (2007) definition. This is a significant limitation of the new definition insofar as the role of marketing as the mechanism for meeting organisational goals is now an assumed or implied role, rather than a formally recognised feature of the discipline.

Exchange theory

The restoration of the role of exchange is a significant difference between the two definitions. One of the resounding criticisms of the difference between AMA (2004) and AMA (1985) was the removal of the exchange concept from the marketing definition. Although exchange could be implied in the AMA 2004 definition, it has been restored to formally recognise the historical foundation of marketing as an exchange based paradigm. Exchange is now incorporated as a part of the process of creation, communication and delivery of an offering of value, which incorporates aspects of coproduction into the marketing definition.

Exchange as an activity or process for developing offerings of value recognises the evolution of applications of marketing. This approach incorporates the business to business relationships which are orientated to just-in-time production, electronic data interchange and co-creation of solutions. Similarly, it allows for the incorporation of the services dominant logic approach of co-created service delivery as a mechanism of exchange between customer and the embedded or actual service.

Finally, it also allows for the incorporation of the dynamic of the Web2.0 and new media marketing where the creation of conversation and dialogue has replaced the traditional one way communications approach of non-interactive media. Overall, reintroducing exchange as a companion to the creation, communication and delivery of offerings of value recognises the importance of integrating the customer's role as creator-consumer, whilst maintaining the importance of the steps required to be undertaken by the organisation to present an offering of value to the market.

AMA (2007) and Exchange Theory

The AMA (2007) definition also embodies the complexity of exchange theory as outlined by Bagozzi (1975) at the levels of direct exchange, indirect exchange, and complex exchange between marketer, customer/client and society. These dynamics are outlined as follows:

- Marketer <-> Customer/Client: this is the classic one to one commercial marketing exchange between marketer and customer. Direct benefit is sustained by ongoing relationships between the marketer and the organisation
- Customer/Client <-> Society: which is where the market offerings which create value for the customer also create value for the society when consumed by the customer/client. Whilst this exchange of value is not under the direct auspices of marketing, it is an aspect of ethical marketing that the creation, communication, delivery and exchange of value should consider the impact of the use of the market offering for the broader society.

- Partners <-> Society: which is where the creation, communication, delivery and exchange of market offerings is beneficial to society through economic gain, information, broader access to beneficial information and/or dissemination of goods, services or ideas of value.
- Partners <-> Customer <-> Society <-> Partners: which is where all parties are gaining direct and indirect value from the market offerings.
- Partner -> Customer -> Society -> Partner: this transaction is an application of the extended exchange principle of A to B to C to A that is traditionally associated with social marketing and non profit marketing where benefit to the marketer is gained from society as a result of society benefiting from the client/customer's adoption of the market offerings. No direct benefit accrues to the marketer from the client's adoption of the market offerings, however, the marketer, as part of society, receives an indirect benefit as part of the extended model of value exchange.

Customer Relationships

In the AMA's own words, the 2004 definition had elevated customer relationship management (CRM) from a tactical option in direct marketing to a core principle. The AMA's interpretation of their definition did not place the relationship marketing concept into the core of marketing. Instead, they believed that they had incorporated a tactical element of direct mail and database marketing into the core of the discipline. This represents one of the major separations between American Marketing Association and the Euro-Australian schools. Australian and New Zealand marketing practitioners and academics place greater emphasis on the Nordic School of relationship marketing, and were interpreting the AMA (2004) "managing customer relationships" as reflective of the Grönroos (1994) relationship marketing ideology.

On face value, the AMA (2007) definition is more supportive of marketing as a transaction rather than long term relationship. The AMA (2007) definition has no explicit recognition of long term customer relationships, or the principle of marketing as a series of ongoing relationships. It is possible to incorporate the Gronrossian method of customer relationship as a form of offering of value, which would implicitly incorporate the relationship marketing into the creation, delivery and exchange of offerings that have value. However, this is an interpretative inclusion which, whilst not explicitly rejected by the 2007 definition, is equally not explicitly recognised. However, it should be noted that relationship marketing as understood by the Nordic School was not an explicit part of the 2004 definition under the AMA's own interpretation.

Offerings of Value

The shift from "goods, services and ideas" to "value" has been revised as the AMA introduced the concept of "offerings that have value". This approach retains some of the elements of the AMA (1985) "goods, services and ideas" approach insofar as the output of the creation, communication, delivery and exchange process are "offerings that have value".

One criticism of this approach is the emphasis on the "offerings" which can be seen to be production orientated insofar as the offerings are the outcome of a process conducted away from the customer. In contrast, a holistic interpretation of the definition would see the incorporation of exchange as a recognition that the offerings of value are created through a process of negotiation between the marketer and the marketplace. Similarly, the offerings are defined as having value for the customers, clients, partners and society at large which is closer to Dev and Schultz (2004) SIVA approach than it is to McCarthy's (1960) marketing mix.

Four Target Groups of Marketing

Perhaps the most complex, and most likely to be misinterpreted section of the new definition has been the decision to expand the parameter of "customers" and stakeholders into four separate beneficiary groups. Although stakeholders are no longer directly identified as beneficiaries of marketing in the AMA (2007) definition, their needs are contained within the categories of customer, client, partner and society at large. Incorporating the four targeted recipients integrates the value for benefit exchange concept, along with the value for society aspect of the rising trend for corporate social responsibility. It should be noted that marketing is not required to meet the needs of all four elements simultaneously – for example, value for customers in a commercial transaction does not need to give benefit to the allusive (or non existent) non commercial client of the firm. The reclassification of the stakeholders into the four respective targets of marketing is illustrated in Table 2

Table 2: Stakeholders, Stakeholder Context and the AMA (2007) recipients of "Offerings that have value"

AMA (2007)	Stakeholder	Primary Context
Customers/Clients	Customers	Consumption
Partners	Board of Directors	Production
Partners	Creditors and Financiers	Production
Partners	Distributors	Production
Partners	Employees	Production
Partners	Managers	Production
Partners	Shareholders	Production
Partners	Suppliers	Production
Partners	Unions	Production
Society at Large	Competitors	Environment
Society at Large	Government	Regulation and Control
Society at Large	Local Community	Environment
Society at Large	Media	Environment
Society at Large	Social Pressure Lobby Groups	Environment
Society at Large	Society / Citizens / Community	Environment

The four target recipients of the offerings that have value are clustered into the four stakeholder contexts insofar as the consumption context represents customers and clients, society at large represents the environment and regulation/control context, and the production context stakeholders are the "partners". This is supported by definition of production context stakeholders as (Chapter 3) everyone involved in sourcing the component parts for making the product (e.g. suppliers), being part the organisation (investors, boards of directors, shareholders, employees), or providing the distribution networks (distributors)

Criticisms of AMA (2007)

Any change to the status quo will bring the probability of benefit and the possibility of negative consequences. In the case of the newly minted marketing definition, there are five negative consequences which are:

- the loss of the opportunity for relationship marketing
- the change of purpose of marketing,
- instability and the speed of change.
- the continued absence of planning as a marketing function
- the need for inclusion by implication

Relationship Marketing versus the management of customer relationships

The absence of relationship management from the AMA (2007) closes the door on the brief period of either direct response tactics (Berry, 1983) or long term relationships of trust, reciprocity and commitment (Gronroos, 1994). Although the transition from AMA (2004) to AMA (2007) served a purpose in highlighting the ideological and linguistic barrier between the different schools of thought in the marketing community, it remains a lost opportunity for moving marketing from transaction to long term relationship.

The Change of Purpose

The AMA has ended the role of marketing as the provider of solutions for the organisation through mutual objective matching (AMA, 1985) or direct organisational benefit (AMA (2004). Although it is possible to interpret "partner" as inclusive of the organisation, this is not the mutual benefit of AMA (1985)'s "satisfy individual and organisational objectives" nor is reflective of the AMA (2004) requirement for benefit for the organisation and the stakeholders. Whilst broadening the base of marketing in a manner that is more inclusive for the variety of non commercial roles marketing plays in the modern economy, there is still a need for commercial marketing to have a focus on meeting the needs of the organisation through profit, sales or other objectives.

Although 'partners' can been deliberately interpreted to represent the organisation, suppliers, distributors and other parties involved in the production stakeholder context, this remains an implied and implicit aspect of the modern definition. Similarly, exchange of

value between partners and client / customers is interpreted to provide a context in which to incorporate the direct organisational benefit of meeting organisational goals through satisfying customer requirements at a profit, rather than being a recognised or explicit element of the definition.

Whilst the broad base suits certain sub disciplinary areas such as non profit, political and social marketing, it must be acknowledged that any definition of marketing needs to reflect the commercial realities of the discipline. Having a fundamental flaw in the recasting of the role of marketing away from a problem solver / solution provider for organisational needs may result in a further redefinition of marketing back towards the exclusionary direct benefit orientation of 2004. This will increase the instability of the discipline if a further patch, upgrade and new definition is launched.

Instability and the Speed of Change

Whilst the AMA (2004) definition had its critics, and certainly had flaws and weaknesses, it was given less than three years of operational life before being replaced. The speed of change is noteworthy – marketing has remained reasonably constant in the definition over time with the first official definition of commercial marketing in 1935, refined in 1985 and again a third time in 2004. The half life of transition through marketing definitions at a intervals of fifty years, twenty years and now three years threatens to leave the current definition with a life expectancy of only a few months. The central binding definition that represents the core discipline and is adapted out into the sub disciplinary areas needs a greater level of stability than has been presented since the turn of the century. By the end of the first decade of the new millennium, marketers will have operated under three separate definitions of marketing, which indicates a potential instability in the disciplinary structure.

The continued absence of planning

One of the hidden casualties of the AMA (2004) definition had been the recognition of the role of marketing as a "process of planning". In the AMA (1985) definition, marketing was concerned with both aspects of long term planning and the more immediate aspects of execution of the marketing mix. Although the AMA (2007) can be interpreted as referencing marketing planning through the activities and processes aspect of the definition, the continued absence of planning as part of the definition casts doubts on the long term orientation of marketing. Further, combining the absence of planning with the reluctance to move towards the relationship marketing orientation, it could be argued that marketing is moving too far towards a short term transaction orientation where it has the role of implementation, and limited or no contribution to the long term planning or goal setting of the organization.

The need for inclusions by implication

The alternative ways and means of interpreting a definition allowed many marketers to take the AMA (2004) definition, and include key aspects of marketing theory as implied components of the greater whole. For example, marketers chose to argue that exchange was implicit in the concept of value, and therefore, unnecessary as part of the formal definition,

and still incorporated as an implied aspect of marketing. However, implied inclusion relies on the interpreter of the definition understanding that non-explicit elements exist, and further relies on those implicit components having been taught or explained to them. In interpreting the definition for this chapter, numerous components of marketing including marketing planning, market orientation, and the value of long term relationships versus short term transactions have been included by interpretation rather than being part of the formal definition.

Praise for the AMA (2007)

Whilst there are reasons to criticise the new marketing definition, the changes between AMA (2004) and AMA (2007) have also brought benefits for marketing. Three immediately identifiable areas are the recognition of non-customer recipients of marketing outputs, the revival of exchange theory, and the recognition of co-creation of value through customer-customer exchange

Clients ▸ ▸ ▸ ▸

When the AMA initially released their draft version of the marketing definition to AMA members for endorsement, specific mention was made of the need to recognise the marketing activities undertaken by non-profit and social marketing did not always involve "customers", and as such, the AMA included "clients" as an explicit endorsement of the work of the non-commercial arm of marketing. Overt recognition and endorsement of the sub disciplinary areas was also supported by the incorporation of the changes to the definition that ensured the non-commercial arms were not disadvantaged by an overly financial/economic return driven definition.

Complex Exchange ▸ ▸ ▸ ▸

AMA (2007) does more than just restore exchange to the definition of marketing by incorporating it as part of the process of creating, communicating and delivering value. The contemporary definition recognises the complex exchange pattern of marketing as a series of smaller exchanges through a network of offerings of value between customer/clients, partners and the society at large. This recognition and use of Bagozzi's (1975) complex exchange theory gives the AMA (2007) definition an extra level of compatibility with the traditional indirect benefit approach of social marketing. Further, the inclusion of value exchange between customers, and/or partners and/or society is recognition of the co-creation of value by the end users.

Co creation of symbolic value ▸ ▸ ▸ ▸

The new definition recognises the creation, communication and delivery of value through the exchange of symbolic meaning for brands, ideas, and behaviours which strengthens the applicability of the marketing process to social marketing (McCracken, 1989). Co-creation

of value through either services or embedded services has been a hallmark of the service dominant logic (Vargo and Lusch, 2004) whereby the value is created through the customer's use of a product or service. The AMA (2007) definition builds on the co-creation platform by recognising inter-customer exchange as a means of creation, communication and delivery of value which can be utilised by social marketing for developing community driven solution, social norms, cultural and symbolic meanings for brands, and the interpretation of social marketing messages into ideas, values and beliefs.

Conclusion

Changes to the formal definition of marketing recognise marketing as a dynamic and living discipline which constantly changes in light of changing business practices. The modification of the AMA definition between 2004 and 2007 came about primarily due to criticisms of the content and process by which the 2004 definition was developed. Using a more inclusive and consultative process the 2007 definition addresses many of these criticisms by explicitly re-introducing core foundations of marketing including the exchange paradigm, whilst adopting elements of the 2007 expanded conceptualisation of marketing activity. Whilst stakeholders and relationship marketing had only a brief appearance in formal definitions, their impact is still real in day to day marketing activity. Stakeholders have been replaced with the broad categorisation of the recipients of marketing while a broad interpretation of "value" can encompass the importance of not only gaining, but retaining customers.

The AMA with its flagship publication, Journal of Marketing remains the most influential organisation world wide in the promotion of marketing theory and practice. However "marketing", both as a management practice and academic discipline, has reached a level of maturity where it cannot be considered in monolithic terms. Increasingly new applications of marketing are leading to new schools of marketing thought such as the Nordic school of relationship marketing and the emergence of services-dominant logic. Regardless of these developments, there is still a need for a succinct definition of marketing which is broad enough to provide a general framework for theory and practice while simultaneously providing boundaries which clearly delineate its reach.

New definitions of marketing will continue to emerge. This is part of the strength of the marketing discipline and recognises its connection to management practice, consumers and therefore, its ongoing value and relevance to business.

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